

THE INTERNAL REVENUE SERVICE'S USE OF  
PRIVATE DEBT COLLECTION COMPANIES TO  
COLLECT FEDERAL INCOME TAXES

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HEARING  
BEFORE THE  
COMMITTEE ON WAYS AND MEANS  
U.S. HOUSE OF REPRESENTATIVES  
ONE HUNDRED TENTH CONGRESS  
FIRST SESSION

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MAY 23, 2007

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**WEDNESDAY, MAY 23, 2007**

**U.S. HOUSE OF REPRESENTATIVES,  
COMMITTEE ON WAYS AND MEANS,  
*Washington, DC.***

The Committee met, pursuant to notice, at 10:12 a.m., in room 1100, Longworth House Office Building, Hon. Charles B. Rangel (Chairman of the Committee), presiding.

[The advisory announcing the hearing follows:]

# ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

FOR IMMEDIATE RELEASE  
May 23, 2007  
FC-12

CONTACT: (202) 225-1721

## Chairman Rangel Announces Hearing on Internal Revenue Service's Use of Private Debt Collection Companies to Collect Federal Income Taxes

House Ways and Means Committee Chairman Charles B. Rangel today announced that the Committee will hold a hearing on the Internal Revenue Service's use of private debt collection companies to collect Federal income taxes. **The hearing will be held on Wednesday, May 23, 2007, in 1100 Longworth House Office Building, beginning at 10 a.m.**

In view of the limited time available to hear witnesses, oral testimony will be from invited witnesses only. Witnesses at the hearing will include representatives of the Internal Revenue Service (IRS), National Taxpayer Advocate, U.S. Government Accounting Office, National Treasury Employees Union, and contractors involved in the collection of Federal income taxes. However, any individual or organization not scheduled for an oral appearance may submit a written statement for consideration by the Committee and for inclusion in the printed record of the hearing.

### BACKGROUND:

On March 22, 2007, Committee Chairman Rangel launched an investigation into the IRS's use of private debt collection companies citing complaints from taxpayers, instances of harassment and violations of law, and the inability of taxpayers to hold the Federal Government liable for the actions of a collection contractor. Further, Chairman Rangel urged the Commissioner not to proceed with awarding additional contracts.

The Committee will focus on issues related to whether: (1) Federal income tax collection is a fundamental governmental function and, as such, should not be contracted to the private sector as a profit-making venture; (2) the IRS can collect Federal income taxes more efficiently and effectively than private debt collection companies; (3) taxpayers are subject to confusion, questionable private debt collection company tactics, harassment, and abuse due to the use of private debt collectors; (4) adequate options are available to the IRS to address uncollected taxes in the accounts receivable inventory; (5) the program is ready for expansion and new private debt collection contracts should be awarded in the coming months; and (6) Internal Revenue Code section 6306 should be repealed.

In announcing the hearing, Chairman Rangel stated: **"The IRS use of private companies to collect Federal income taxes is an affront to the integrity of our tax system. The collection of Federal taxes is a basic governmental function and one that should not be assigned to profit-making businesses. The outsourcing of IRS tax collection to the private sector carries an unacceptable large risk that taxpayer rights will be trampled and their personal identities stolen. It is unacceptable that taxpayers are footing the bill for a program that pays private companies up to a 25 percent bounty when the IRS can do the same job for pennies on the dollar."**

### FOCUS OF THE HEARING:

As part of the American Jobs Creation Act of 2004 (P.L. 108-357), the Congress enacted Internal Revenue Code section 6306 authorizing the IRS to enter into contracts with debt collection companies for the purpose of collecting Federal income

taxes. The provision allows for the IRS to pay a commission of up to 25 percent of amounts collected. Last year, the IRS awarded contracts to three debt collection companies: Pioneer Credit Recovery, Inc., The CBE Group, Inc. and Linebarger Goggin Blair and Sampson, LLP. In September 2006, the three companies began contacting taxpayers and collecting Federal income taxes. After six months, the IRS renewed contracts for two of the companies. The IRS intends to award additional contracts in late 2007.

The use of private debt collectors for Federal income tax purposes continues to be controversial. The IRS Taxpayer Advocate, various consumer interest groups, IRS employees, and others have expressed concern that the use of private companies to collect Federal taxes is inappropriate and that the tax law provision should be repealed. Others, including private debt collection companies, have argued that the private debt collectors collect money that would go uncollected.

#### **DETAILS FOR SUBMISSION OF WRITTEN COMMENTS:**

**Please Note:** Any person(s) and/or organization(s) wishing to submit for the hearing record must follow the appropriate link on the hearing page of the Committee website and complete the informational forms. From the Committee homepage, <http://waysandmeans.house.gov>, select "110th Congress" from the menu entitled, "Committee Hearings" (<http://waysandmeans.house.gov/Hearings.asp?congress=110>). Select the hearing for which you would like to submit, and click on the link entitled, "Click here to provide a submission for the record." Once you have followed the on-line instructions, completing all informational forms and clicking "submit" on the final page, an email will be sent to the address which you supply confirming your interest in providing a submission for the record. You **MUST REPLY** to the email and **ATTACH** your submission as a Word or WordPerfect document, in compliance with the formatting requirements listed below, by close of business **Wednesday, June 6, 2007**. Finally, please note that due to the change in House mail policy, the U.S. Capitol Police will refuse sealed-package deliveries to all House Office Buildings. For questions, or if you encounter technical problems, please call (202) 225-1721.

#### **FORMATTING REQUIREMENTS:**

The Committee relies on electronic submissions for printing the official hearing record. As always, submissions will be included in the record according to the discretion of the Committee. The Committee will not alter the content of your submission, but we reserve the right to format it according to our guidelines. Any submission provided to the Committee by a witness, any supplementary materials submitted for the printed record, and any written comments in response to a request for written comments must conform to the guidelines listed below. Any submission or supplementary item not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All submissions and supplementary materials must be provided in Word or WordPerfect format and **MUST NOT** exceed a total of 10 pages, including attachments. Witnesses and submitters are advised that the Committee relies on electronic submissions for printing the official hearing record.
2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.
3. All submissions must include a list of all clients, persons, and/or organizations on whose behalf the witness appears. A supplemental sheet must accompany each submission listing the name, company, address, telephone and fax numbers of each witness.

Note: All Committee advisories and news releases are available on the World Wide Web at <http://waysandmeans.house.gov>.

The Committee seeks to make its facilities accessible to persons with disabilities. If you are in need of special accommodations, please call 202-225-1721 or 202-226-3411 TTD/TTY in advance of the event (four business days notice is requested). Questions with regard to special accommodation needs in general (including availability of Committee materials in alternative formats) may be directed to the Committee as noted above.

Chairman RANGEL. The hearing will come to order. We want to thank all of our witnesses that have been consolidated into one panel to expedite the hearing, and to share with the Internal Revenue Service that many Members of Congress have received many complaints from their constituents as a result of their decision to designate private debt collectors in lieu of collectors that work for, and have been are trained by, the Internal Revenue Service. I think it is generally accepted that there is a special relationship between taxpayers and the Internal Revenue Service, and I think that relationship is violated when it is turned over to entrepreneurs who get paid based on the amount of money that they are able to extract from the taxpayer.

In addition to that, there are some rights of privacy that are involved that many of us believe are very special to that relationship between the Internal Revenue Service and the taxpayers. So, today we are going to explore what has been going on, probably make some changes. What I would like to do is yield to the Ranking Member, Jim McCrery, for purposes of making an opening statement, and then yield whatever time I may have to the Chairman of the Subcommittee on Oversight, John Lewis, who has had extensive hearings in this area.

Mr. McCrery.

Mr. MCCRERY. Thank you, Mr. Chairman. I will make brief comments and then as you will, I will yield to my Ranking Member of the Subcommittee for further opening remarks. I think what we will find today is some mixed testimony about some of the tactics and so forth, but I would urge all of us to listen carefully to everything that is said today, either by the witnesses or by submitted testimony that could be written or oral and make sure that we listen to everything and not just pieces or parts. I think that will give us a good view of the reality of this situation, and I look forward to hearing the witnesses and being able to probe a little more deeply into some of these issues surrounding this, and at this time Mr. Rangel if you want to yield to your Chairman, then I will yield to my Ranking Member.

Chairman RANGEL. Thank you. Let me first thank John Lewis and his staff for the excellent job they have done in looking into this issue on behalf of the Congress, and we look forward to your statement, Mr. Lewis.

Mr. LEWIS. Well, thank you very much, Mr. Chairman. Thank you for holding this hearing today. Today, Mr. Chairman, the Committee is repeating history. We are again reviewing whether private debt collectors should be used to collect Federal taxes. This is not a new question for the Committee on Ways and Means. Mr. Chairman, I have in my hand a copy of the record of the Committee on Ways and Means from 1874. This is a report of the Committee. This is not something that I am making up. It came from the Library locked up, and one of our staff members found this report. The Committee, in 1874, repealed the authority to use private tax collectors, and as stated in that report, in this report, the Committee is the opinion that any system of framing the collection of any portion of the revenue of the government is fundamentally wrong. No necessity for such laws exist. The Internal Revenue Bureau is possessed of foreknowledge of the laws relating to the col-

lection of the revenue and has all the machinery necessary for their full and complete enforcement. The Committee, in view of the facts, believe that the law should be repealed and the contract made the reunder should be revoked and annulled.

These words are true today 130 years later. The collection of Federal income taxes is a core government function. Let me repeat. The collection of Federal income taxes is a core government function. It is the mission and purpose of the IRS. Today's program can never work. Taxpayers and the American public deserve better. To date, the collectors have made nearly 1 million calls in attempt to reach 35,000 taxpayers. Those calls have been subject to harassment, confusion and abuse. Mr. Chairman, I ask that a partial list of taxpayer complaints be included in the record.

Chairman RANGEL. Without objection.

Mr. LEWIS. Mr. Chairman, I also want to play five calls between an IRS private collector and one taxpayer. I want all of my colleagues to hear what our constituents are facing as the private collectors attempt to find the correct person owing taxes. Asked that the transcript of these calls be included in the record and that we play them for the members to hear.

Chairman RANGEL. Without objection.

[The prepared statement of Mr. Lewis follows:]

**Opening Statement of Congressman John Lewis (D-GA)**  
**Committee on Ways and Means**  
**Hearing on**  
**Internal Revenue Service's Use of**  
**Private Debt Collection Companies to**  
**Collect Federal Income Taxes**  
**May 23, 2007**

Today, the Committee is repeating history. We again are reviewing whether the Treasury Department should be allowed to contract with private debt collectors for federal taxes.

This is not a new question for the Ways and Means Committee. I would like to read from an 1874 Report of the Committee repealing Treasury's authority to use private tax collectors and pay them a commission. It states:

The Committee are of opinion that any system of farming the collection of any portion of the revenue of the Government is fundamentally wrong . . . No necessity for such laws exist . . . the Secretary of the Treasury and the head of the Internal Revenue Bureau are empowered by law to make all collections of taxes . . . The Internal Revenue Bureau is possessed of full knowledge of the laws relating to the collection of the revenue . . . [and] has all the machinery necessary for their full and complete enforcement . . . The Committee, in view of the facts . . . believe that the law . . . should be repealed and the contracts made thereunder should be revoked and annulled.

H.R. REP. NO. 559, 43d Cong., 1st Sess. 9 (1874).

These words are true today—130 years later.

The collection of federal income taxes is a core government function. It is the mission and purpose of the Internal Revenue Service.

Today's private collector program can never work. Taxpayers and the American public deserve better.

- Debt collectors receive up to a 25% bounty on federal income taxes.

- The IRS has 45 employees watching 90 contract employees yet no one has the full story on what they are doing.
- The IRS depends on the collectors to “self-report” complaints of taxpayers.
- GAO investigators have confirmed that contractors have been exercising discretion over who gets offered to take the customer satisfaction survey.
- The program targets low- and middle-income taxpayers rather than those who have the means to protect themselves.
- At the end of the day, most Americans don’t even know that the harassing calls they receive are from debt collectors hired by the IRS.

To date, the collectors have made nearly one million calls in attempts to reach 35,000 taxpayers. Those called have been subject to harassment, confusion, and violations of taxpayer protections.

Mr. Chairman, I ask that a partial list of taxpayer complaints be included in the record. (These materials are attached to my opening statement.)

Mr. Chairman, I also would like to play five calls between an IRS private collector and one taxpayer. I want my colleagues to hear what our constituents are facing as the private collectors attempt to find the correct person owing taxes. I ask that a transcript of these calls be included in the record and that we play them for the Members to hear.

The “cat and mouse” game you are about to hear has captured over 300,000 members of the public. All but 10,000 of these were innocent parties who did not owe any tax. Social security numbers along with tax information must be protected to prevent identity theft and ensure the integrity of our tax system.

I ask, “Who is in charge here?” What have we done? We must end this.

Now, I ask that the audio be played.

Mr. LEWIS. The cat and mouse game you are about to hear had caught over 300,000 members of the public over the last 6 months. All but 10,000 of these were innocent parties who did not owe any tax. Social Security numbers, along with tax information, must be protected to prevent identity theft and ensure the integrity of our tax system. I ask who is in charge here, what have we done. We must end this. Now, Mr. Chairman, I ask that the audio be played.

Chairman RANGEL. At this time however I would like to yield to Mr. Ramstad—

[Audio starts.]

We will suspend the time on this presentation and recognize Mr. Ramstad, the Ranking Member of the Committee that had hearings on this subject matter.

Mr. RAMSTAD. I thank the Chairman for calling this hearing, and I thank the Ranking Member for yielding. As we all know, Congress granted the IRS authority to contract with private collection agencies to bring in taxes owed for two principle reasons. First of all, to improve enforcement in a proven way to boost compliance by tax delinquents and second to promote fairness for Americans who already paid their share of the tax burden.

We should not allow the actions of tax deadbeats to continue unchecked, and I think everyone agrees, we need to close the tax gap in this country. By helping to reduce uncollected Federal tax liabilities, this program does just that. It has already been proven to help close the tax gap. During the next 10 years, in fact, the program is projected to collect between \$1.5 billion and \$2.2 billion that would otherwise go uncollected, to continue to widen the tax gap. After commissions that can yield up to \$2 billion of revenue toward closing the tax gap. This program certainly does not diminish the important work of IRS employees. In fact, it allows IRS employees to focus their attention on more difficult cases that require their expanded enforcement efforts while the private collection agencies focus on lower priority cases, cases in which the taxpayers already have admitted they owe the tax.

Each and every case here, there is an admission by the taxpayer of tax liability. After a competitive procurement process, background checks and other safeguards were put in place in this statute. The first cases were assigned for private collection September of last year. Since then, just since September of 2006, close to \$20 million has been collected. This is money again that would otherwise go uncollected. This program is also boosting other IRS enforcement efforts. The IRS, in fact, may retain up to 25 percent of the amount collected for additional collection enforcement activities. Given the parameters in which the IRS is operating, the service has already retained close to \$4 million in new funds for collection activities, and it may receive more than \$500 million during the next 10 years. This is real money that is being saved the American taxpayer.

The private debt collection program has been carefully developed with extensive oversight from the IRS, and I commend the Commissioner and the service for that oversight. Private collection agencies are held to the same high standards for the protection of taxpayer rights as IRS employees. I would like to later answer some of the allegations and the anecdotal evidence that we saw

earlier. But we all know that violations of taxpayer rights—if taxpayers are violated in this process, they can result in large fines and even imprisonment under the statute.

So, we need to enforce the law if there are abuses. In fact, private collection agents have an additional layer of liability because they could be sued under the Fair Debt Collection Practices Act unlike, of course, IRS employees.

Given the sensitive nature of this work, Congress must have information about the operations of the program. What is working, what is not working, what needs to be fixed or improved. That is the reason I believe for this hearing today. As the IRS oversight board noted last week, the program seems to be working well. Those are their words, the board's words. But it should continue to be monitored closely, also the board's words, and I don't think anybody on this dais or in this room would disagree.

Mr. Chairman, let me close by saying since the Treasury Inspector General for tax administration is not represented here today, I ask unanimous consent that the March 27, 2007 report, entitled The Private Debt Collection Program Was Effectively Implemented But Some Follow-Up Actions Are Still Necessary be submitted for the record.

Chairman RANGEL. Without objection.  
[The information follows:]

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**TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION**



***The Private Debt Collection Program Was  
Effectively Developed and Implemented, but  
Some Follow-up Actions Are Still Necessary***

March 27, 2007

Reference Number: 2007-30-066

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

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DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

March 27, 2007

**MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED  
DIVISION**

**FROM:** *Michael R. Phillips*  
Michael R. Phillips  
Deputy Inspector General for Audit

**SUBJECT:** Final Audit Report – The Private Debt Collection Program Was  
Effectively Developed and Implemented, but Some Follow-up Actions  
Are Still Necessary (Audit # 200630022)

This report presents the results of our review of the Internal Revenue Service's (IRS) Private Debt Collection program (Program). The overall objective of this review was to evaluate the effectiveness of the IRS' implementation of the Program.

***Impact on the Taxpayer***

To implement the Program, the IRS will use private collection agencies (hereafter referred to as PCAs or contractors) as an additional resource to help collect delinquent Federal taxes. In July 2004, the Department of the Treasury estimated the IRS will collect \$1.4 billion through the Program over the next 10 years (Fiscal Years 2006-2015). Balance-due cases were first placed with three contractors on September 7, 2006. Overall, the IRS effectively developed and implemented several aspects of the Program, thus providing better assurance that taxpayer rights are protected and Federal tax information is secure. Specifically, contractor employees were adequately trained, background investigations were completed, telephone call monitoring and oversight procedures were established, and computer and physical security procedures were established before cases were assigned. However, the IRS needs to follow up on computer security issues, update procedure guides, and update the application used to calculate projected revenue.



***The Private Debt Collection Program Was  
Effectively Developed and Implemented,  
but Some Follow-up Actions Are Still Necessary***

***Synopsis***

As of September 30, 2006, the gross accounts receivable to the IRS totaled \$271 billion. On October 22, 2004, the President signed the American Jobs Creation Act,<sup>1</sup> which created a new Internal Revenue Code Section 6306 (2004) to permit PCAs to help collect Federal tax debts.

Overall, the IRS has taken proactive measures to effectively develop and implement the Program.

- The IRS took appropriate steps to ensure contractor employees received sufficient and adequate training on applicable laws and regulations before allowing them access to Federal tax information. This included providing contractors with an orientation and overview of the training required and conducting an onsite assessment of the contractor training.
- The IRS required all contractor employees assigned to the Program contract, or who have access to Federal tax information, to undergo background investigations. The IRS granted either interim or final approval of background investigations for each employee working on the contract at the time of our review.
- The IRS established adequate oversight through telephone call monitoring, case action reviews, taxpayer satisfaction surveys, and a variety of other reviews to ensure contractors adhere to contract requirements and protect taxpayer rights.
- The IRS took appropriate and sufficient steps to ensure development and implementation of the Program were effective throughout the process. The IRS met regularly with the contractors to address concerns and issues, tested contractor systems for readiness and accuracy, and evaluated contractor computer and physical security.
- At the IRS' request, the Treasury Inspector General for Tax Administration Office of Investigations participated in various implementation areas such as creating a training video for the contractors, participating in onsite contractor training, and reviewing various security issues.

Concurrent to our review, the IRS performed its own tests and analyses to identify and address risks and concerns. After our audit work was completed, the IRS continued to monitor the PCAs and, on February 14, 2007, announced the contracts for two of the PCAs had been extended through March 8, 2008. The agency decided, and the third PCA agreed, that their contract would not be extended.

While we identified several issues during implementation, the IRS resolved most concerns prior to the initial placement of cases with the contractors. Nonetheless, some issues still need to be

<sup>1</sup> Pub. L. No. 108-357, 118 Stat. 1418 (2004).



***The Private Debt Collection Program Was  
Effectively Developed and Implemented,  
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addressed. One contractor maintained Federal tax information on a computer server that was also used to maintain data for four other contractor clients. Use of a shared server increases the risk that Federal tax information may be inadvertently disclosed, lost, or stolen. Although use of a single, dedicated server is not required, we believe this would strengthen security over Federal tax information. One contractor was using Telnet to transmit Federal tax information. This significantly increases the risk that Federal tax information may be inadvertently disclosed or stolen. One contractor had not loaded antivirus software on its operating system or encryption software on its laptops. This significantly increases the risk that Federal tax information may be corrupted or disclosed. At both contractors, we identified computer security concerns about the protection of Federal tax information and audit trails. While the security concerns are not as significant as those noted previously, improvements could be made to better enhance computer security. Many of the computer security issues identified, including the maintenance of data on a shared server, were risks identified at the location of the contractor for which the IRS did not extend the contract.

We also identified physical security concerns at both contractors that presented various weaknesses. By the time we had concluded our onsite reviews, the contractors were in the process of resolving some of the computer and physical security concerns. We were subsequently notified by the contractors that they had resolved most of the concerns.

Some sections in the Program guides and handbooks need to be strengthened and/or clarified. If procedures are not updated, these conditions could result in untimely suspension of contractor collection action, unsatisfactory customer service, and unidentified or untimely identified taxpayer complaints.

One contractor used an initial contact script that provided its employees with a very specific set of questions to ask the taxpayer. Another contractor used a series of general questions and a checklist of specific items for the employees to consider. The third contractor did not use an initial contact script and relied upon training provided to employees to ask the appropriate questions. There was no requirement for contractors to have scripts. However, we believe taxpayer rights would be better protected if contractors were required to use scripts for all types of telephone contacts with taxpayers and provide the scripts to the IRS, which could then review and approve them.

Finally, the IRS hired a contractor to develop a revenue model and used this model to calculate projected revenue based on the inventory the IRS plans to place with contractors. The IRS is in the process of updating this model and the revenue projection goals, and we identified three additional areas that we believe management should consider during this update. The IRS should consider the impact of those taxpayers who opt out of the Program; the age of the cases that will be assigned to the contractors; and the actual percentage of dollars being collected, which was projected to be higher than those achieved by collection agencies used by other Federal Government agencies.



***The Private Debt Collection Program Was  
Effectively Developed and Implemented,  
but Some Follow-up Actions Are Still Necessary***

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**Recommendations**

We recommended the Director, Collection, Small Business/Self-Employed Division, include in the Request for Quotation<sup>2</sup> a requirement for PCAs to maintain Federal tax information on a separate server; follow up to ensure PCAs have completed their efforts to resolve the specified computer and physical security concerns; update the Contracting Officer's Technical Representative<sup>3</sup> and Telephone Monitoring and Case Action Review procedures to ensure consistency and completeness; include in the Request for Quotation a requirement for PCAs to provide a copy of scripts for all telephone contacts with taxpayers to the IRS, which will then review and approve them; and continue updating and/or modifying the revenue model to ensure the IRS appropriately accounts for the impact of taxpayers who opt out of the Program, the age of the balance due, and the actual collection rate achieved.

**Response**

The IRS agreed with our recommendations and will address security issues in the next contract negotiations and PCA security reviews, update policies to provide consistent and complete instructions regarding taxpayer complaints, strengthen control of taxpayer contacts, and address concerns in the revised revenue model. Management's complete response to the draft report is included as Appendix V.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Daniel R. Devlin, Assistant Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-5894.

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<sup>2</sup> A Request for Quotation is a formal solicitation to sources outside of the Federal Government for offers to provide products or services.

<sup>3</sup> Contracting Officer's Technical Representatives are responsible for managing the PCA contracts and ensuring compliance with requirements.



***The Private Debt Collection Program Was  
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***The Private Debt Collection Program Was  
Effectively Developed and Implemented,  
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### ***Abbreviations***

COTR	Contracting Officer's Technical Representative
IRS	Internal Revenue Service
PCA; contractor	Private collection agency



***The Private Debt Collection Program Was  
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but Some Follow-up Actions Are Still Necessary***

### ***Background***

As of September 30, 2006, the gross accounts receivable to the Internal Revenue Service (IRS) totaled \$271 billion. To help address this tax debt inventory, the Department of the Treasury proposed that Congress pass legislation authorizing the IRS to use private collection agencies (hereafter referred to as PCAs or contractors) to help collect tax debts for simpler types of cases. The IRS refers to this effort as the Private Debt Collection program (Program).

*One objective of the Private Debt Collection program is to use private collection agencies to help collect the \$271 billion in taxes owed to the Federal Government.*

On October 22, 2004, the President signed the American Jobs Creation Act,<sup>1</sup> which created a new Internal Revenue Code Section (§) 6306 (2004) to permit PCAs to help collect Federal tax debts. The law allows PCAs to locate and contact any taxpayer specified by the IRS, to request from such taxpayer full payment of the amount of Federal tax due, and to obtain financial information with respect to such taxpayer. The law allows the IRS to retain and use an amount not in excess of 25 percent of the amount collected by the PCAs for the cost of services performed under a contract and an amount not in excess of 25 percent of the amount collected for collection enforcement activities of the IRS.

According to the IRS, the three main objectives of the initiative to use contractors are to:

- Help to significantly reduce the growing number of uncollected tax liabilities.
- Help maintain taxpayer confidence in the fairness of the tax system by assisting the IRS in addressing more of its delinquent accounts.
- Assist the IRS in its continued focus to dedicate existing collection and enforcement resources on more difficult cases and issues.

The legislation provides that the provisions of the Fair Debt Collection Practices Act<sup>2</sup> shall apply to PCAs. The law also prohibits PCAs from committing any act or omission that IRS employees are prohibited from committing in the performance of similar services. The legislation created Internal Revenue Code § 7433A (2004) to permit civil actions by taxpayers for unauthorized collection actions by employees of the PCAs. The law also amended § 1203 of the IRS

<sup>1</sup> Pub. L. No. 108-357, 118 Stat. 1418 (2004).

<sup>2</sup> 15 U.S.C. §§ 1601 note, 1692-1692o (2000).



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Restructuring and Reform Act of 1998<sup>3</sup> relating to termination of employment for misconduct to include employees of PCAs, if such individuals committed any act or omission described under subsection (b).

According to the IRS, contractors will be required to adhere to all taxpayer protections and will be prohibited from threatening or intimidating taxpayers, or otherwise suggesting that enforcement action will or may be taken, if a taxpayer does not pay the liability. The contractors must also adhere to all security and privacy regulations for systems, data, personnel, and physical security, and all taxpayer rights protections.

On March 9, 2006, the IRS awarded contracts to 3 firms from a field of 33 for the first phase of the Program. On September 7, 2006, the IRS placed an initial inventory of 11,562 balance-due accounts with the 3 contractors.

This review was performed in the IRS Small Business/Self-Employed Division in New Carrollton, Maryland, and the contractor worksites of Pioneer Credit Recovery, Inc. in Perry, New York; Linebarger Goggan Blair & Sampson, LLP in Austin and San Antonio, Texas; and The CBE Group Inc. in Waterloo, Iowa, during the period April through December 2006. The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

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<sup>3</sup> Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).



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### ***Results of Review***

#### ***The Internal Revenue Service Has Taken Proactive Measures to Effectively Develop and Implement the Private Debt Collection Program***

Overall, the IRS effectively developed and implemented several aspects of the Program before cases were assigned to the contractors. These include contractor employee training, background investigations, and IRS oversight of the contractors.

- **The IRS conducted an orientation and overview of the required training and other contract assistance needed for all contractor employees working on the Program.** This event provided the contractors an opportunity to raise questions and clarify requirements. As observers of the event, we believe the IRS presenters were fully prepared and well versed in their subject areas. Overall, the orientation attendees expressed satisfaction with the training and the instructors. The attendees were then responsible for providing training sessions to their employees who were to be assigned IRS cases.
- **The IRS conducted onsite assessments of the training sessions to ensure contractor employees were trained on the applicable laws and regulations.** Topics required to be covered included the Fair Debt Collection Practices Act, IRS Restructuring and Reform Act of 1998 § 1203, and disclosure. The IRS reported the contractors conducted training sessions from August 8 through 30, 2006. Contractor employees were required to pass with a 70 percent or better rating in every examination taken. Those not passing were not allowed to work IRS cases or continue with the training. The IRS documented the contractors took appropriate actions to remove such employees from working on the contract.
- **The IRS Personnel Security and Investigation Program office granted either interim or final approval of background investigations for all the contractor employees working on the contract at the time of our review.** Contractors are required to submit to the IRS requests for background investigations for all employees assigned to work on the contract. On two separate occasions, we requested current lists of contractor employees working on the contract: one prior to and one subsequent to the placement of cases. We forwarded the lists to the Personnel Security and Investigation Program office to determine the status of the background investigations. Upon reviewing the response, we confirmed that contractor employees are not permitted to work on the private debt collection contract until approval has been granted. Also, we confirmed employees



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whose approvals were denied had been appropriately and timely removed from working on the contract.

- **The IRS established an adequate method to monitor the quality of work being performed by the contractors.** The proposed IRS oversight, designed to ensure contractors adhere to contract requirements and the protection of taxpayer rights, includes telephone call monitoring and case action reviews by quality analysts, taxpayer satisfaction surveys, and a variety of reviews by the Contracting Officer's Technical Representatives (COTR).<sup>4</sup>
- **The IRS ensured it and the contractors were appropriately prepared.** The IRS conducted regular meetings to plan and determine the status of implementation and to address concerns and issues; ran tests of the contractors' systems to determine readiness and verify accuracy; conducted computer and physical security reviews at each contractor worksite; and established an independent review team to review contractor safeguards, processes, and procedures and to evaluate risks.
- **The IRS engaged the Treasury Inspector General for Tax Administration Office of Investigations in the process.** The Office of Investigations participated in various implementation areas such as creating a training video for the contractors, participating in onsite contractor training, and reviewing various security issues.

Concurrent to our review, the IRS performed its own tests and analyses to identify and address risks and concerns. After our audit work was completed, the IRS continued to monitor the PCAs and, on February 14, 2007, announced the contracts for two of the PCAs had been extended through March 8, 2008. The agency decided, and the third PCA agreed, that their contract would not be extended.

While we identified several issues during implementation, the IRS resolved most concerns prior to the initial placement of cases with the contractors. Only a small number of issues still need to be addressed.

***Many Computer and Physical Security Concerns Have Already Been Addressed***

We conducted independent computer and physical security reviews at the worksites of two of the three contractors awarded contracts to work on the IRS Program. We also participated as third-party observers of the IRS review of physical security at the worksite of the third contractor.

<sup>4</sup> COTRs are responsible for managing the PCA contracts and ensuring compliance with requirements.



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Overall, we believe the contractors implemented a strong system of computer and physical security controls. However, we identified the following concerns that presented a risk to security. Except where noted, the concerns relate to only one particular contractor. Our onsite reviews were conducted prior to the placement of cases with the contractors; therefore, the contractors had not yet received Federal tax information.

***Maintaining data on a shared server increases the risk of disclosure, loss, and theft of Federal tax information***

One of the contractors we reviewed used a separate, dedicated server<sup>5</sup> to maintain Federal tax information. The other contractor we reviewed maintained Federal tax information on a server that was also used to store data for four other contractor clients. Using a shared server increases the risk that Federal tax information may be inadvertently disclosed, lost, or stolen. Contractors are required to ensure all account data are, at a minimum, partitioned off from other data maintained on their computer systems. While a single, dedicated server for Federal tax information is not required, we believe Federal tax information should be maintained on a separate server to adequately protect against unauthorized disclosure while on a contractor's computer system. Subsequent to our onsite review, the IRS informed us it verified the contractor had properly partitioned account data on its system.

The contractor that used the shared server used Telnet and Secure Shell to transmit Federal tax information. We have security concerns about the contractor's decision to use Telnet. This compounds our concern over the use of a shared server. Telnet is a network protocol used on the Internet or local area network connections. It is considered unsecure due to various security vulnerabilities. Secure Shell is a set of standards and an associated network protocol that allows users to establish a secure channel between a local and a remote computer. Secure Shell, which provides greater security, was designed to replace Telnet.

There are three main reasons why Telnet is not recommended for modern systems from the point of view of computer security:

- Commonly used Telnet daemons<sup>6</sup> have several vulnerabilities discovered over the years, and several more probably still exist.
- Telnet lacks an authentication scheme<sup>7</sup> that would make it possible to ensure communication is carried out between the two desired hosts and not intercepted in the middle.

<sup>5</sup> A server is a computer on a network (a group of two or more computers) that manages network resources.

<sup>6</sup> A daemon is a computer program that runs in the background, rather than under the direct control of the user.

<sup>7</sup> An authentication scheme is a method of verifying the sender and/or receiver (host) of a data transmission, to ensure the data have not been intercepted or altered.



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- Telnet, by default, does not encrypt<sup>1</sup> data sent over the connection, thereby allowing intercepted data to be easily read and later used for malicious purposes.

Contractor management informed us they use Telnet because their other clients who share the server with the IRS need Telnet to run their applications. However, using Telnet to transmit data significantly increases the risk that Federal tax information may be inadvertently disclosed or stolen. We were later informed by contractor management that they had resolved this issue by developing the procedure to implement Secure Shell prior to the activation of Telnet when transmitting data. Although Secure Shell was not designed to be used in conjunction with Telnet, we believe this technique is sufficient to address our concern. However, the contractor did not indicate whether it uses this technique when transmitting data to its other clients. Because we had not considered this procedure during our onsite review of computer security, we cannot report on the risks associated with the contractor transmitting data to its other clients using a different technique.

**Antivirus and encryption software are needed to provide an additional layer of security**

We noted, as did a contractor hired by the IRS to review computer security, that one PCA had not loaded antivirus software on its operating system. We also noted the same PCA had not loaded encryption software on the laptops of 16 individuals authorized to enter the worksite. At the time of our review, the PCA had been unable to locate antivirus software compatible with its operating system. Also, although PCA management's anticipated completion date for laptop encryption was subsequent to our onsite review, the IRS indicated the PCA agreed not to allow the laptops to be removed from the worksite until after the software had been loaded.

Contractors are required to ensure all Federal tax information is protected from unauthorized disclosure while on their computer systems and to protect and maintain the integrity of their systems. Contractors should employ virus protection mechanisms at essential information system entry and exit points (e.g., firewalls, routers, remote-access servers) and at workstations or servers on the network. Contractors should update virus protection mechanisms (including the latest virus definitions) when new releases are available.

Antivirus software is an additional layer of security needed to protect an operating system from viruses and worms. Encryption software would protect data from unauthorized disclosure in case a laptop is lost or stolen. When antivirus and encryption software are not installed, the risk that Federal tax information may be corrupted or disclosed increases significantly.

We were later informed by PCA management that they had loaded encryption software on their laptops. Also, although they stated they had not obtained antivirus software for their operating

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<sup>1</sup> Encryption is the process of converting data into a secret code. To read an encrypted file, a user must have access to a password that enables him or her to decrypt the data.



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system, they indicated the issue was addressed with the IRS by implementing other security measures within the Windows environment and by physically and logically locking the system down to prevent the loading of any software onto the system.

**Contractors enhanced computer security by addressing various concerns**

We identified the following concerns related to the protection of Federal tax information and audit trails. Each concern listed below is specific to either one or the other of the contractors we reviewed. While we do not consider these concerns to be as significant as the issues identified above, improvements could be made to enhance computer security.

1. An unnecessary service on the router had not been disabled.
2. There is no method in place for tracking system issues.
3. Two risks identified by a contractor hired by the IRS to review computer security have not been properly addressed by the PCA.
4. Audit logs have not been properly protected.
5. Access control lists have not been applied to the CISCO<sup>9</sup> switch.<sup>10</sup>
6. Backup tapes are not marked as Federal tax information and stored separately.
7. The contractor has not completed development of a policy to address the IRS' concern regarding contractor managers having access to email.
8. User accounts are not disabled timely.

These concerns could permit inappropriate access to the system, inappropriate user capabilities, and unauthorized disclosure. Although we believe these issues need to be addressed, we did not consider them significant enough risks to prevent the assignment of cases to the contractors.

Contractors are required to implement system security controls, safeguards, and mechanisms at all levels of the system and application layers. Settings of information technology products must be configured to the most restrictive mode consistent with information system operational requirements. Also, the information system must be configured to provide only essential capabilities and specifically prohibit and/or restrict the use of unnecessary functions, ports,<sup>11</sup> protocols,<sup>12</sup> or services. Access to Federal tax information is to be restricted to only those persons whose duties or responsibilities require access; thus, information shall be clearly labeled "Federal tax data." Additionally, to avoid inadvertent disclosures, Federal tax information shall be kept separate from other information.

<sup>9</sup> CISCO is a leading manufacturer of network equipment.

<sup>10</sup> A switch is a device that filters and forwards data files between computers within a network.

<sup>11</sup> A port is an access point into and out of a computer. The ports on a computer or server are used to connect to communications lines and modems.

<sup>12</sup> A protocol is a convention or standard that controls or enables the connection, communication, and data transfer between two computing endpoints.



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While management of each contractor was in the process of addressing some of the concerns listed previously, the remaining concerns were not considered or were simply overlooked. By the time we concluded our onsite reviews, contractor management was in the process of addressing concerns 2, 4, 5, and 6. We were later informed by management of each contractor that they had resolved all of their respective issues. Many of the computer security issues discussed above, including the maintenance of data on the shared server, were risks identified at the location of the PCA for which the IRS did not extend the contract.

**Contractors promptly resolved physical security concerns**

The contractors implemented numerous physical security controls. Examples include requiring employees to wear photo identification badges, controlling entry through key cards, securing the work area with an alarm system, positioning video cameras at entrances, installing slab-to-slab perimeter walls, and requiring visitors to obtain authorization prior to entering the work area. Although several strong controls were in place, we identified a number of concerns at each contractor worksite that we believe weakened physical security. Appendix IV includes a list of the specific concerns.

In developing and implementing physical security controls, contractor management simply overlooked these particular factors while focusing on other security measures. However, contractor management immediately addressed our physical security concerns as we identified them. By the time we had concluded our onsite reviews and briefed IRS management on our results, all but one of the concerns had been addressed. Because contractor management believed differentiating identification badges posed a security risk for their employees, they deferred the issue to the IRS for its consideration and agreed to implement any changes the IRS deemed necessary. Differentiating identification badges is not a requirement. However, due to the existence of a secondary, unmonitored entrance, we believe implementing this action would strengthen access controls. We were later informed by management of the respective contractor that they had resolved this issue.

***Recommendations***

The Director, Collection, Small Business/Self-Employed Division, should:

**Recommendation 1:** Include in the Request for Quotation<sup>13</sup> a requirement for PCAs to maintain Federal tax information on a separate, dedicated server when the IRS expands the Program to include additional contractors.

**Management's Response:** The IRS agreed with the recommendation. The Director, Collection, Small Business/Self-Employed Division, will include in the next Request for

<sup>13</sup> A Request for Quotation is a formal solicitation to sources outside of the Federal Government for offers to provide products or services.



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Quotation, a requirement for PCAs to maintain Federal tax information on a separate, dedicated server.

**Recommendation 2:** Follow up to ensure the contractors have completed their efforts to resolve computer and physical security concerns including implementing Secure Shell prior to the activation of Telnet when transmitting data, loading encryption software onto laptops, disabling the unnecessary service on the router, tracking system issues, protecting audit logs, applying access control lists, labeling backup tapes as Federal tax information and storing them separately, developing an email policy, timely disabling user accounts, and using differentiated identification badges.

**Management's Response:** The IRS agreed with the recommendation. The Director, Collection, Small Business/Self-Employed Division, will follow-up with the PCAs to ensure all computer and physical security issues listed in the recommendation have been resolved.

***Handbooks and Guides Were Revised to Address Most Concerns  
Regarding Procedural Consistency and Completeness***

The IRS developed several handbooks and guides for the Program. These documents provide the procedures necessary to carry out the requirements of the Program contract. In reviewing the procedures, we noted the following areas that needed to be strengthened and/or clarified.

**Security procedures for handling taxpayer complaints could be strengthened**

Taxpayer complaints regarding a contractor may be received either verbally or in writing from a taxpayer or third party, self identified by a contractor, or identified by an IRS employee.

In evaluating draft procedures to determine whether the IRS had developed effective steps to handle taxpayer complaints, we identified some noncritical areas that needed to be addressed by management. The IRS was still in the process of perfecting the procedures at the time we reviewed them.

- Despite Referral Unit<sup>14</sup> procedures to inform taxpayers that someone from the IRS will contact them regarding complaints, the COTR procedures identify only one occasion when taxpayers will be contacted. The COTR will respond to taxpayers if a written complaint is received for a Type One<sup>15</sup> complaint. However, there were no procedures

<sup>14</sup> The IRS Referral Unit is responsible for assigning cases to contractors; maintaining cases; recalling cases; responding to inquiries from taxpayers, contractors, and IRS staff; and handling taxpayer complaints.

<sup>15</sup> Complaints are assigned a type code, based on the severity of the allegation(s). Rude behavior would be a Type One complaint, intimidation would be a Type Two complaint, and a violation of the Fair Debt Collection Practices Act would be a Type Three complaint.



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for contacting taxpayers when verbal complaints are received or when written Type Two or Type Three taxpayer complaints are received.

- The COTR procedures did not identify a time period for forwarding taxpayer complaints to the contractors.
- Procedures for the Telephone Monitoring and Case Action Reviews conducted by the IRS did not provide specific steps for reviewers to identify and report taxpayer complaints. Also, if a reviewer identifies an error or problem, which would include a taxpayer complaint, the procedures directing the reviewer to forward issues to the COTR once a week were not consistent with other procedures to forward complaints to the COTR either immediately or within 24 hours of receipt.

The Government Accountability Office *Standards for Internal Control in the Federal Government* require significant events to be clearly documented. At the time we conducted our review, IRS management was already in the process of revising procedures for the Telephone Monitoring and Case Action Reviews to include steps for reviewers to identify and handle taxpayer complaints. However, procedures still do not direct reviewers to immediately forward taxpayer complaints to the COTR. Also, recently revised COTR procedures do not address the issues noted above. If procedures are not updated, these conditions could result in untimely suspension of contractor collection action, unsatisfactory customer service, and unidentified or untimely identified taxpayer complaints.

**The IRS clarified contractor procedures for suspending collection**

The draft PCA Policy and Procedures Guide did not provide procedures to suspend contractor collection action when the following conditions occur:

- During Referral Unit review of installment agreement<sup>16</sup> requests within the contractor's authority.
- When a taxpayer appeals a rejected installment agreement.
- When a contractor receives a verbal threat(s) from a taxpayer.
- Upon receipt of a taxpayer lawsuit referencing an account assigned to a contractor.

These conditions are identified as events warranting suspension of PCA collection action in various other IRS Program procedure guides. Without clarification of procedures, contractors may not suspend collection action timely on accounts with these conditions. However, after we presented this information to IRS management, the PCA Policy and Procedures Guide was revised to resolve all four issues.

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<sup>16</sup> An installment agreement allows taxpayers to pay tax liabilities by making regular payments to the IRS over time rather than all at once.



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***Recommendation***

**Recommendation 3:** The Director, Collection, Small Business/Self-Employed Division, should update the COTR procedures to identify a time period for forwarding taxpayer complaints to the PCAs and for contacting taxpayers regarding verbal taxpayer complaints and written Type Two and Type Three taxpayer complaints. Also, the Telephone Monitoring and Case Action Review procedures should be updated to direct analysts to immediately forward taxpayer complaints to the COTR.

**Management's Response:** The IRS agreed with the recommendation. The Director, Collection, Small Business/Self-Employed Division, will update the COTR and Quality Assurance Handbooks to incorporate instructions for responding to taxpayer complaints to address the issues identified in the recommendation.

***Contractors Were Not Required to Have Scripts for Employees to Use When Contacting Taxpayers***

The Request for Quotation did not require the contractors to have a script to direct employees through telephone conversations with taxpayers. However, if the contractor used an initial contact script, the IRS reviewed and approved the questions and procedures. One contractor used an initial contact script that provided its employees with a very specific set of questions to ask the taxpayer. Another contractor used a series of general questions and a checklist of specific items for the employees to consider. The third contractor did not use an initial contact script and relied upon training provided to employees to ask the appropriate questions.

The IRS reviewed the initial contact scripts for the two contractors and asked one of the contractors to change the script and it was appropriately changed. We reviewed the changed scripts and determined the questions were appropriate and none of the questions violated taxpayers' rights. However, we believe taxpayer rights would be better protected if the Request for Quotation required the contractors to use a script for all types of telephone contacts and provide them to the IRS, which could then review and approve the scripts for every contractor. This would also result in consistent approaches that the contractors take in contacting taxpayers and better allow the IRS to perform a more consistent quality review, including the monitoring of telephone calls. The IRS plans to expand the Program and issue a new Request for Quotation in May 2007 soliciting more contractors.

***Recommendation***

**Recommendation 4:** The Director, Collection, Small Business/Self-Employed Division, should include in the Request for Quotation a requirement for PCAs to provide a copy of scripts for all telephone contacts with taxpayers to the IRS, which will then review and approve them.



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**Management's Response:** The IRS agreed with the recommendation. The Director, Collection, Small Business/Self-Employed Division, will include in the next Request for Quotation a requirement for PCAs to provide a copy of scripts for all telephone contacts with taxpayers to the IRS for review and approval.

***The Internal Revenue Service Should Continue Monitoring Revenue Projection Goals***

The Department of the Treasury budget process requires annual revenue estimates for tax proposals.<sup>17</sup> A revenue estimate serves as a benchmark for measuring the effects of tax law changes and is generally over a 10-year period. In July 2004, the Department of the Treasury calculated a \$1.4 billion estimate in revenue over the next 10 years (Fiscal Years 2006-2015) for the tax proposal that permits contractors to help collect Federal tax debts.

The IRS hired a contractor to develop a revenue model and used this model to calculate projected revenue based on the inventory the IRS plans to place with contractors. The IRS continuously compared its inventory plans and revenue estimates to the Department of the Treasury estimates through February 2006. The IRS revenue model estimates many factors, including:

- Standard Collection Curve – The model applies a standard collection industry curve for each case placement over a 12-month period to determine the number of cases on which some or all tax due was collected.
- Referrals for Enforcement – Estimated number of cases returned to the IRS for enforcement action.
- Unresolved Service Accounts (Recalls) – Estimated number of cases returned to the IRS due to other reasons (e.g., hardship,<sup>18</sup> innocent spouse<sup>19</sup>).
- Administrative Resolutions – Estimated number of cases returned to the IRS due to death or bankruptcy of the taxpayer.
- Initial Ramp Up – The model shows a gradual increase in the assigned collection rate<sup>20</sup> to allow the IRS and contractors to reach optimum performance and productivity.

We evaluated the revenue model to determine whether the IRS' plans based on the model were sufficient to achieve the goals set by the Department of the Treasury. The IRS is in the process of updating the model and the revenue projection goals. To ensure revenue estimates are accurate, we believe management should consider the following three issues when updating the revenue projection goals.

<sup>17</sup> A tax proposal is a bill considering a change or modification to a provision of the Internal Revenue Code.

<sup>18</sup> A hardship means the taxpayer currently has no ability to pay the taxes.

<sup>19</sup> An innocent spouse is a taxpayer that can be relieved of responsibility for paying tax, interest, and penalties if his or her spouse (or former spouse) improperly stated or underpaid the tax.

<sup>20</sup> The collection rate represents the percentage of dollars collected in comparison to the total balance due of the cases placed with the contractors.



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**Revenue projection does not account for the impact of taxpayers who opt out of the Program**

The IRS will be sending letters notifying taxpayers that their accounts have been assigned to a contractor. Included with these letters is *What You Can Expect When the IRS Assigns Your Account to a Private Collection Agency* (Publication 4518), which informs taxpayers they may submit a written request to opt out of the Program if they do not wish to work with a PCA.

The revenue model does not include a factor to estimate the number of taxpayers who will elect to opt out of the Program. The IRS indicated the ability for taxpayers to opt out is a unique factor that has never been accounted for by either Federal Government agencies or private industry. Therefore, there are no historical data on which to base an estimate to include in the model.

Until the cases are assigned, the impact of taxpayers who elect to opt out of the Program cannot be predicted. Therefore, as the IRS expands into assigning other types of cases to contractors, the impact of taxpayers who opt out of the Program should be reexamined. While few taxpayers have initially opted out, the number may increase as accounts assigned to contractors become more complex.

**Criterion has been adjusted to include older cases in the contractor inventory**

The IRS has been continuously monitoring inventory levels for initial implementation of the Program. The contractor provided the IRS with an interactive revenue model used for long-range planning. The revenue model allows the IRS to change the inventory selection criteria and determine the impact to projected revenue. The IRS reexamined inventory options and changed case criteria to maximize revenue projections and make sure it has enough inventory available to meet the capacity of the contractors. One change to the contractor inventory involved increasing the age a case has been in an IRS collection status. The initial Program criterion called for cases that had been in collection status for less than 1 year; however, the age in status was increased to 2 years and then to 3 years.

The amount of time a case is in an IRS collection status is not the true age of the account liability; it is the length of time the account has been assigned to that particular collection status. We previously reported<sup>21</sup> that, when the criterion for age in collection status was less than 1 year, 72 percent of the cases available for placement in the Program were more than 2 years old. Now that the length of time in collection status has been increased, the cases being assigned are probably even older. We reported that older debts are frequently more difficult to collect; thus the change in case age criterion may limit the IRS' ability to reach the Department of the Treasury's revenue goals for the Program. Management agreed the cases being assigned to the

<sup>21</sup> Management Needs to Continue Monitoring Some Case Selection Issues As the Private Debt Collection Program Is Implemented (Reference Number 2006-30-064, dated April 2006).



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contractors may be older but stated the contractors are willing to work the cases being assigned while the IRS does not have the resources to work them.

***The collection rate used by the IRS is higher than the industry standard***

During the research phase of the Program, the IRS visited some Federal and State Government agencies that have used contractors, to assess their best practices for tax collection. The Federal Government agencies visited were the Department of the Treasury Financial Management Service and the Department of Education; the State agencies included some in New Jersey, Michigan, Georgia, Maryland, and Virginia. During the visits, the IRS obtained data from the Department of Education and the Financial Management Service on their collection rates with contractors; these data reflect an average collection rate of less than 3 percent. The IRS did not request collection rate figures from the State agencies. However, the State of California has announced it has referred more than \$2 billion to private debt collection companies over the past 17 years, and \$50 million (less than 3 percent) was actually recovered.<sup>22</sup> Our research of the Department of Education and Financial Management Service confirmed the collection rate of 3 percent.<sup>23</sup>

The IRS discussed the potential inventory selected for assignment with subject-matter experts to determine the estimated collection rates used in its revenue model. The revenue model starts with a lower collection rate and gradually increases it to a range of 10 percent to 15 percent of the contractor inventory. This "ramp-up" factor, as previously stated, allows the IRS and contractors time to reach optimum performance and productivity. As of December 31, 2006, the contractors had collected \$11.4 million of the \$105 million in liabilities placed with them by the IRS. This represents a collection rate of 10.5 percent. Based on the ramp-up factor, this rate should continue to increase.

Other Federal and State Government agencies work balance-due cases for approximately 180 calendar days before turning them over to contractors; however, the IRS is being very selective in the cases it assigns to contractors. For the initial phase, the cases placed are individual taxpayers who have filed a tax return with a balance due.

Considering these factors, the IRS contractor collection rate should be higher than that achieved by other Federal and State Government agencies. Management plans to adjust the collection rate once the cases are worked by the contractors and data are available to determine a true collection rate for types of cases. The IRS recognizes it will need to continuously monitor the collection rate as it expands the types of cases assigned to contractors to work.

<sup>22</sup> *The Tax Man and the Debt Collector Team Up* (MSN Money, September 2005).

<sup>23</sup> Department of Education data relate to contractor performance from contract inception through June 2002. Financial Management Service data relate to contractor referrals and collections as of April 2003.



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***Recommendation***

***Recommendation 5:*** As data become available, the Director, Collection, Small Business/Self-Employed Division, should continue updating and/or modifying the revenue model to ensure the IRS appropriately accounts for the impact of taxpayers who opt out of the Program, the age of the balance due, and the actual collection rate achieved.

***Management's Response:*** The IRS agreed with the recommendation. The Director, Collection, Small Business/Self-Employed Division, will begin a review of the revenue model in July 2007 and either construct a new revenue model or update the existing model based on actual performance. The updated or revised model will be available in November 2007.



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**Appendix I**

***Detailed Objective, Scope, and Methodology***

The overall objective of this review was to evaluate the effectiveness of the IRS' implementation of the Private Debt Collection program (Program). To accomplish this objective, we:

- I. Evaluated the revenue projection goals and determined if the IRS' plan was sufficient to achieve the goals.
- II. Identified the methods established to transmit Federal tax information and evaluated the procedures used to transmit data between the IRS and the contractors.
- III. Evaluated controls established to ensure taxpayer rights are protected.
  - A. Determined if and how contractor employees were trained on the applicable laws and regulations and if the contractors certified in writing that the required training had been provided.
  - B. Obtained and evaluated the Quality Assurance program established to monitor contractor activities to ensure there are no violations.
  - C. Determined if the IRS developed an effective program to handle taxpayer complaints.
  - D. Identified situations in which contractors are required to stop collection action and determined if procedures were in place.
- IV. Evaluated the proposed physical and data security controls over Federal tax information.
  - A. Determined if a background investigation had been conducted on all contractor personnel working on the contract and if any employee who failed the background investigation had been barred from working on the contract with the IRS.
  - B. Made physical visits to each of the three contractor worksites. At two of the worksites, we evaluated the adequacy of the physical security to be provided over Federal tax information. At the third worksite, we sat in as third-party observers while the IRS evaluated the adequacy of the physical security.
  - C. Determined if the contractors implemented effective physical security safeguards to ensure protection of the information technology system. We determined if the computer systems processing, storing, and transmitting Federal tax information met or exceeded controlled access protection audit trails, identification/authentication controls, and access controls.



***The Private Debt Collection Program Was  
Effectively Developed and Implemented,  
but Some Follow-up Actions Are Still Necessary***

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- D. Analyzed the IRS' plan to review the physical and data security at the contractors' worksites.
- V. Determined the method the IRS developed to monitor the quality of work being performed by the contractors and evaluated the adequacy of the proposed IRS oversight over the Program.



***The Private Debt Collection Program Was  
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**Appendix II**

***Major Contributors to This Report***

Daniel R. Devlin, Assistant Inspector General for Audit (Small Business and Corporate Programs)  
Parker F. Pearson, Director  
Amy L. Coleman, Audit Manager  
Todd M. Anderson, Lead Auditor  
Christina M. Dreyer, Senior Auditor  
Michelle Griffin, Senior Auditor  
Denise M. Gladson, Auditor



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### **Appendix III**

#### ***Report Distribution List***

Commissioner C  
Office of the Commissioner – Attn: Chief of Staff C  
Deputy Commissioner for Services and Enforcement SE  
Deputy Commissioner, Small Business/Self-Employed Division SE:S  
Director, Collection, Small Business/Self-Employed Division SE:S:C  
Project Director, Filing and Payment Compliance Modernization, Small Business/Self-Employed Division SE:S:C:FPCMO  
Chief Counsel CC  
National Taxpayer Advocate TA  
Director, Office of Legislative Affairs CL:LA  
Director, Office of Program Evaluation and Risk Analysis RAS:O  
Office of Internal Control OS:CFO:CPIC:IC  
Audit Liaison: Commissioner, Small Business/Self-Employed Division SE:S



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**Appendix IV**

***Physical Security Concerns***

Prior to placement of cases with the contractors, we identified the following physical security concerns during our onsite reviews of contractor worksites. Except where noted, each concern is specific to one contractor. Management of each contractor immediately addressed our physical security concerns as we identified them.

1. Perimeter doors did not have adequate locking mechanisms.
2. Two rooms were not wired to the alarm system.
3. The main entrance to the IRS work area was not monitored by a receptionist.
4. Identification badges of employees working on the contract were not differentiated from identification badges of unauthorized employees that work across the hall.
5. At both contractor worksites, the visitor log was not reviewed to determine each visitor's need for access.
6. Six employees had keys to the IRS work area; one did not have a need for access to Federal tax information.
7. On a couple of occasions, private mail service companies inappropriately delivered IRS contract-related mail to the contractor's headquarters office located in the building next door.
8. Employees were permitted to use their desk telephones for personal calls.
9. Vendors were provided escorted access to the collection room.
10. There were plans to provide one employee with control over both the unassigned key cards and the system that controls the access levels of the key cards.
11. One employee was responsible for control over misdirected remittances.
12. Procedures for handling significant conditions or situations that affect business operations had not been updated for computer security and had not been developed for physical security.

Concerns 1-6 represent a weakness in restricting access. Concerns 6-9 represent a weakness in preventing unauthorized disclosure. Concerns 10 and 11 represent a weakness in providing a separation of duties. Concern 12 represents a weakness in handling security breakdowns.

Contractors are required to provide secured collection office facilities and equipment to perform tasks under the private debt collection contract. The specified area shall be restricted to authorized IRS and contractor employees, and the area shall be physically separated from other activity with walls and secured access per IRS security requirements. The facility must have a locked and alarmed perimeter. Additionally, access to the space must provide an audit trail such as a sign-in log, card reader, or computerized mechanical lock.



***The Private Debt Collection Program Was  
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**Appendix V**

***Management's Response to the Draft Report***



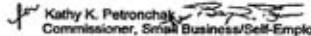
DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

RECEIVED

MAR 26 2007

March 23, 2007

**MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT**

FROM:  Kathy K. Petronchak,   
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report – The Private Debt Collection Program  
Was Effectively Developed and Implemented, but Some  
Follow-up Actions Are Still Necessary  
(Audit No. 200630022)

We have reviewed the draft report titled, "The Private Debt Collection Program Was Effectively Developed and Implemented, but Some Follow-up Actions Are Still Necessary."

I am pleased the report acknowledges our efforts to establish a productive Private Debt Collection (PDC) program that conforms to security standards and meets our high customer service expectations. The report confirms that we adequately prepared the Private Collection Agencies (PCA) to handle federal tax information and to work with taxpayers to resolve balance due accounts. We have been diligent in our efforts to hold the PCAs to high standards for the protection of taxpayer rights and privacy.

This project is already delivering positive results and exceeding expectations. On September 7, 2006, we transferred our first cases to the PCAs. As of February 2007, we had placed 30,822 cases with the PCAs and they have collected over \$14 million. Using conservative projections, the IRS is on track to recover the costs of developing and implementing this program in 2008.

The recommendations in this report are consistent with our ongoing efforts to perfect our policies and procedures. We agree with all recommendations and will include them in our planned enhancements. We will address security issues in the next contract negotiations and PCA security reviews; update policies to provide consistent and complete instructions regarding taxpayer complaints; strengthen control of taxpayer contacts; and address TIGTA's concerns in the revised revenue model.



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Attached is a detailed response outlining our planned corrective actions. If you have any questions, please contact me at (202) 622-0600 or Deborah Wolf, Project Director, Filing and Payment Compliance Modernization, Small Business/Self-Employed, at 609-278-7732.

Attachment



***The Private Debt Collection Program Was  
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Attachment

**RECOMMENDATION 1:**

The Director, Collection, Small Business/Self-Employed Division should include in the Request for Quotation a requirement for PCAs to maintain Federal tax information on a separate, dedicated server when the IRS expands the program to include additional contractors.

**CORRECTIVE ACTION:**

We agree that requiring PCAs to maintain Federal tax information on a separate, dedicated server will enhance data security. In the next Request for Quotation, we will include a requirement for PCAs to maintain Federal tax information on a separate, dedicated server.

**IMPLEMENTATION DATE:**

July 15, 2007

**RESPONSIBLE OFFICIAL(S):**

Director, Filing & Payment Compliance Modernization Office

**CORRECTIVE ACTION MONITORING PLAN:**

We will monitor the corrective action as part of our internal management control system.

**RECOMMENDATION 2:**

The Director, Collection, Small Business/Self-Employed should follow-up to ensure the contractors have completed their efforts to resolve computer and physical security concerns including implementing Secure Shell prior to the activation of Telnet when transmitting data, loading encryption software onto laptops, disabling the unnecessary service on the router, tracking system issues, protecting audit logs, applying access control lists, labeling backup tapes as Federal tax information and storing them separately, developing an email policy, timely disabling user accounts, and using differentiated identification badges.

**CORRECTIVE ACTION:**

We agree the IRS should validate that all physical and security issues identified by IRS and TIGTA have been resolved. We will follow-up with the PCAs to ensure all computer and physical security issues listed in this recommendation have been resolved.

**IMPLEMENTATION DATE:**

May 15, 2007

**RESPONSIBLE OFFICIAL(S):**

Director, Filing & Payment Compliance Modernization Office



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**CORRECTIVE ACTION MONITORING PLAN:**

We will monitor the corrective action as part of our internal management control system.

**RECOMMENDATION 3:**

The Director, Collection, Small Business/Self-Employed Division, should update the COTR procedures to identify a time period for forwarding taxpayer complaints to the PCAs, and for contacting taxpayers regarding verbal taxpayer complaints and written Type Two and Type Three taxpayer complaints. Also, the Telephone Monitoring and Case Action review procedures should be updated to direct analysts to immediately forward taxpayer complaints to the COTR.

**CORRECTIVE ACTION:** We agree comprehensive instructions for responding to taxpayer complaints should be included in the COTR and Quality Assurance Handbooks.

1. We will update the COTR Handbook to include a time period for forwarding complaints to the PCA.
2. We will update the COTR Handbook to include instructions on handling verbal taxpayer complaints and written Type Two and Type Three taxpayer complaints.
3. We will update the Quality Assurance Handbook to include procedures on forwarding taxpayer complaints identified during Telephone Monitoring and Case Action reviews to the COTR.

**IMPLEMENTATION DATE:**

June 15, 2007

**RESPONSIBLE OFFICIAL(S):**

Director, Filing & Payment Compliance Modernization Office

**CORRECTIVE ACTION MONITORING PLAN:**

We will monitor the corrective action as part of our internal management control system.

**RECOMMENDATION 4:**

The Director, Collection, Small Business/Self-Employed Division, should include in the Request for Quotation a requirement for PCAs to provide a copy of scripts for all telephone contacts with taxpayers to the IRS, who will then review and approve them.

**CORRECTIVE ACTION:**

We agree that the use of approved telephone scripts by the PCAs would improve customer service and ensure consistent taxpayer treatment. We will include in the next Request for Quotation a requirement for PCAs to provide a copy of



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scripts for all telephone contacts with taxpayers to the IRS for review and approval.

**IMPLEMENTATION DATE:**

July 15, 2007

**RESPONSIBLE OFFICIAL(S):**

Director, Filing & Payment Compliance Modernization Office

**CORRECTIVE ACTION MONITORING PLAN:**

We will monitor the corrective action as part of our internal management control system.

**RECOMMENDATION 5:**

As data become available, the Director, Collection, Small Business/Self-Employed Division, should continue updating and/or modifying the revenue model to ensure the IRS appropriately accounts for the impact of taxpayers who opt out of the Program, the age of the balance due, and the actual collection rate achieved.

**CORRECTIVE ACTION:**

We agree that the revenue model should be updated and/or modified as new information becomes available and as changes are made in PCA case inventory. We will begin a review of the revenue model in July 2007 and either construct a new revenue model or update the existing model based on actual performance. Inherent in the collection rate used in the modeling are factors such as opt outs and age of the balance due. The updated or revised revenue model will be available November 2007.

**IMPLEMENTATION DATE:**

November 15, 2007

**RESPONSIBLE OFFICIAL(S):**

Director, Filing & Payment Compliance Modernization Office

**CORRECTIVE ACTION MONITORING PLAN:**

We will monitor the corrective action as part of our internal management control system.

Mr. RAMSTAD. One issue this hearing will explore is whether the collection of taxes is an essential government function, an issue already raised by my distinguished colleagues on the other side. Contrary to the assertion that it is not, a number of Federal and more than 40 State agencies are currently using private collection agencies to collect overdue income taxes and other debts including student loan payments and alcohol and cigarette taxes. So, this private debt collection function is hardly a novel function to be contracted to the private sector. I believe that dismantling the private debt collection program would be a mistake, it would be a step backward in our efforts to close the tax gap, and I hope we don't retreat on that front at this critical juncture. Again, I thank the Chair and I yield back.

Chairman RANGEL. Thank you, Mr. Ramstad. We will now proceed. The first witness will be Nina Olson, National Taxpayer Advocate, Internal Revenue Service. You can present your testimony as you like. You have 5 minutes and your entire statement will be entered into the record by unanimous consent.

**STATEMENT OF NINA OLSON, NATIONAL TAXPAYER  
ADVOCATE, INTERNAL REVENUE SERVICE**

Ms. OLSON. Thank you, Mr. Chairman, Ranking Member Mr. McCrery, and Members of the Committee. Thank you for inviting me today to testify about the IRS' private debt collection initiative. I will limit my oral testimony to five points.

First, there is no good business case for this initiative. Second, there were few very easy cases, IRS collection cases for the private collection agencies or PCAs to work. Third, the IRS collects taxes better than the PCAs. Fourth, the PCA's approach to taxpayers raises significant concerns for tax administration. Fifth, taxes are different from other debts and therefore should not be treated like those other debts.

In May 2003, I appeared before a Ways and Means Subcommittee on Oversight hearing and outlined my concerns about the IRS' then proposal to contract out the collection of certain categories of tax debt to private collection agencies. While in 2003, I had IRS assurances that my concerns would be addressed, as time passed and the IRS implemented the program, my concerns multiplied, not lessened. These concerns led me to call for repeal of the private debt collection authority in my annual report to Congress in 2006. I believe the right approach to any collection case must address dual goals. First, to ensure that the taxpayer is able to comply with the tax laws so as not to exacerbate the noncompliance. Second, to collect the tax after taking into account the taxpayer's particular facts and circumstances.

In my view, PCAs fail at both these goals. PCAs must maximize profit for their shareholders by collecting the most past due dollars at the least expense to the companies. PCAs do not have the ability or the authority to consider the taxpayers' individual circumstances. Such consideration involves the exercise of judgment and discretion and thus cannot be delegated by the government to third parties. The IRS projects that the PDC initiative will bring in between \$1.5 and \$2.2 billion in gross revenue before commissions over 10 years. The midpoint of that 10-year range is \$1.85

billion which translates to an average of \$185 million a year on a gross basis before commissions and IRS administrative costs.

Here is how the gross annualized PDC revenue stacks up to the IRS' most recent annual estimate of the gross tax gap. Now I asked my staff to make the PDC bar glow orange so you can see it better and you can see how successful that was. The IRS estimates that it will spend about \$71 million in startup and outgoing maintenance costs on this program through fiscal year 2007. If we applied the \$71 million and allocated it to the ACS, the Automated Collection System, we estimate that these funds would bring in about \$1.4 billion as compared to the \$19.5 million brought in by the PDC initiative to date.

The IRS estimates that PCAs at a steady state will have a return on investment of 4 to 1. IRS ACS employees on the other hand have a steady state return on investment of 20 to 1. Proponents of the PCA initiative have consistently stated that the IRS has a significant number of accounts in which taxpayers could be induced into paying what they owe by a simple phone call. The mere fact that there may be a substantial pool of cases that effectively result in revenue if only someone contacted the taxpayer does not mean PCAs are best qualified to handle these cases.

The assigned inventory turns out to be far more complex than the IRS ever expected. The cases that come into the taxpayer advocate service from PCAs show that the concept of an easy tax case is a fallacy. We have earned income tax cases, identity theft, innocent spouse penalty and interest abatement foreign tax credit and financial hardship cases.

In fact, the shortage of easy inventory is driving the IRS to assign inventory with the types of complexities that were never intended to be worked by the private collectors. Expanding the inventory beyond the primary criteria to actual ACS cases, cases involving U.S. territories and possessions to business cases, to nonfilers and to older cases decreases the likelihood that the PCAs will be actually able to collect any payment from the taxpayer, increases the likelihood that the PCAs will make mistakes, and increases the likelihood that the PCA will pressure the taxpayer to agree to an unreasonable payment arrangement.

PCAs utilize a psychological technique to collect the maximum amount from taxpayers while IRS collection employees are trained to address the three Cs, cause, cure and compliance, PCAs in their training materials use language like close the deal and psychological pause, the next person to speak loses. We have slides showing quotes from actual training materials. Now we are not selling Florida swampland here and taxpayers are not marks. We are also not in the NBA finals talking about the next person who speaks loses. We are talking about Federal taxes. These are the life blood of government which we ask taxpayers to come forward and pay. The consequences of playing around with taxpayer morale are great. I believe the PDC program risks too much for too little and therefore I would urge Congress to terminate this program now. Thank you.

[The prepared statement of Ms. Olson follows:]

**Prepared Statement of Nina E. Olson, National Taxpayer Advocate,  
Internal Revenue Service**

Mr. Chairman, Ranking Member McCrery, and distinguished Members of the Committee:

Thank you for inviting me to testify today about the Internal Revenue Service's private debt collection (PDC) initiative.<sup>1</sup>

Because there is so much risk to taxpayers and tax administrators inherent in this program, I have personally devoted a large amount of my time since the fall of 2002 to oversight of the PDC initiative. Since 2004, my office has had at least one full-time employee dedicated solely to tracking this initiative, and for prolonged periods, as many as five Taxpayer Advocate Service (TAS) employees have simultaneously tracked different aspects of the program. As a result of this daily involvement, we have concluded that the PDC initiative is a waste of the government's valuable resources and risks much for a potential increase in tax collection that is negligible, at best, and that in reality may be costing the government more than it receives through this program.

In May 2003, I appeared before a Ways and Means Oversight Subcommittee hearing and outlined my concerns about the IRS's then-proposal to contract out the collection of certain categories of tax debt to private collection agencies (PCAs). At that time, I was uncomfortable with the concept, based both on my own experience representing taxpayers before PCAs in state tax disputes and on the problems inherent in the IRS proposal. While in 2003 I had IRS assurances that my concerns would be addressed, as time passed and the IRS implemented the program, my concerns multiplied, not lessened. These concerns led me to call for repeal of the PDC authority under Internal Revenue Code (IRC) § 6306 in my 2006 Annual Report to Congress.<sup>2</sup>

Despite my opposition to the concept of outsourcing Federal tax collection, I want to acknowledge the dedication and hard work of employees in the Department of the Treasury and the IRS in developing and implementing this initiative. At the time the program was developed, senior officials at the Treasury Department asked me to participate in its development, despite my conceptual concerns, to help protect taxpayer rights to the maximum extent possible. More recently, IRS personnel charged with implementing the program have worked tirelessly and in good faith to make the program work, and members of my staff have been included in some of the implementation decisions. These employees have given their all to make the program work, and I want to make clear that my criticism of the program is in no way intended to be a criticism of their work.

**I. Tax Collection Requires the Exercise of Discretion, and Only the Government Is Constitutionally Permitted to Exercise that Discretion.**

**A. The Overriding Objective of IRS Enforcement Actions Should Be to Maximize Long-Term Tax Compliance.**

We are in agreement, of course, that taxpayers who owe back tax debts should be held accountable. As I outlined in my 2006 Annual Report to Congress, however, I am concerned that the current collection strategy of the IRS does not maximize the government's long-term collection of revenue. The IRS's current collection strategy virtually ignores an entire category of collection cases. In fact, the IRS's failure to work these cases is one of the strongest rationales for utilizing private collection agencies (PCAs). But having recognized this shortfall, we still must ask two questions:

- What is the right way to handle these cases?
- What is the most cost effective way to do so?

I believe that the right approach to any collection case must address dual goals: first, to ensure that the taxpayer is able to comply with the tax laws, so as not to exacerbate the noncompliance; and second, to collect the tax after taking into ac-

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<sup>1</sup> The views expressed herein are solely those of the National Taxpayer Advocate. The National Taxpayer Advocate is appointed by the Secretary of the Treasury and reports to the Commissioner of Internal Revenue. The statute establishing the position directs the National Taxpayer Advocate to present an independent taxpayer perspective that does not necessarily reflect the position of the IRS, the Treasury Department, or the Office of Management and Budget. Accordingly, congressional testimony requested from the National Taxpayer Advocate is not submitted to the IRS, the Treasury Department, or the Office of Management and Budget for prior approval. However, we have provided courtesy copies of this statement to both the IRS and the Treasury Department in advance of this hearing.

<sup>2</sup> IRC § 6306(b)(4) authorizes the Secretary of the Treasury to hire PCAs to perform the following functions with respect to the collection of tax:

count the taxpayer's particular facts and circumstances. In my view, PCAs fail at both of these goals. On the first count, the fiduciary duty of a private company is to maximize profits for its shareholders, which can only be achieved here by collecting the most past-due dollars at the least expense to the company. As the PDC initiative is structured, the objective of maximizing current and future compliance does not fit into the business model; PCAs are compensated solely on the basis of collecting past debts. On the second issue, PCAs do not have the ability or the authority to consider the taxpayer's individual circumstances. Such consideration involves the exercise of judgment and discretion, and thus cannot be delegated by the government to third parties.

B. Under the U.S. Constitution, Tax Collection Is Considered an Inherently Governmental Activity and Generally Cannot Be Outsourced.

As early as 1819, the United States Supreme Court recognized that the Federal Government's taxing power is ancillary to its sovereignty. In *McCulloch v. Maryland*, Chief Justice Marshall stated that the power to tax "is an incident of sovereignty, and is coextensive with that to which it is incident."<sup>3</sup> Thus, that power—to assess and collect taxes—is "inherently governmental." The hallmark of an inherently governmental function is one that requires the exercise of discretion in interpreting and executing the law. It is a function that is recognized as "so intimately related to the public interest as to mandate performance by Government employees. . . ."<sup>4</sup> An inherently governmental function cannot be delegated by the government to private parties.<sup>5</sup> A ministerial function, however, may be delegated to private parties.<sup>6</sup>

Within these constitutional parameters, Congress has broad authority to delegate such governmental powers. Such delegations must establish clear standards that detail how and when private parties may exercise government power. The delegating governmental body must conduct sufficient oversight, including the establishment of procedural safeguards, and retain sufficient control over private delegates to ensure against arbitrary or self-serving use of government power. Under such delegations of government authority, private parties are essentially limited to advising the government and performing ministerial acts. Functions involving the exercise of discretion are reserved to the government itself.

Where the Federal Government seeks to delegate the collection of Federal tax debt to private parties, the activities must be limited to those that do not involve the exercise of discretion. The Federal Government must structure the terms of the contract and its implementation so that the government maintains close oversight and control. The head of the delegating agency must retain the authority to resolve disputes, compromise claims or terminate the collection action.<sup>7</sup> Finally, the Federal Government cannot dilute the rights and protections taxpayers otherwise enjoy merely by contracting out certain functions to private parties.

In 1998, the Federal Activities Inventory Reform (FAIR) Act was enacted to encourage competitive sourcing, a process whereby Federal agencies identify commercial functions being performed by the agencies, develop a business case to determine whether the private sector can efficiently compete with the agencies, and if so, determine the most efficient organization to perform the function. However, the law specifically precludes the contracting out of inherently governmental functions.<sup>8</sup> *The IRS and the Office of Management and Budget (OMB) have long considered the col-*

<sup>3</sup> *Marshall v. McCulloch*, 17 U.S. 316, 429 (1819).

<sup>4</sup> OMB Circular No. A-76 § 6(e) (1999). The current version of OMB Circular No. A-76 states that "[a]n inherently governmental activity is an activity that is so intimately related to the public interest as to mandate performance by governmental personnel." OMB Circular No. A-76 (Revised), Attachment A § (B)(1)(a) (May 29, 2003).

<sup>5</sup> *Carter v. Carter Coal Co.*, 298 U.S. 238 (1936).

<sup>6</sup> In the context of interest abatement, the IRS defines a ministerial act as one that does not involve the exercise of judgment or discretion. Treas. Reg. § 301.6404-2(b)(1).

<sup>7</sup> 31 U.S.C. § 3718(a).

<sup>8</sup> Federal Activities Inventory Reform (FAIR) Act of 1998, Pub. L. No. 105-270, 112 Stat. 2362 (codified as amended at 31 U.S.C.A. § 501, Note § 5 (2)(b)) (providing that a function is "inherently governmental" under the statute if it is "so intimately related to the public interest as to require performance by Federal Government employees."). Examples of inherently governmental functions include actions: (1) "to bind the United States to take or not take some action;" (2) "to determine, protect and advance United States . . . interests;" and (3) "to significantly affect the . . . property of private persons." Id.

*lection of taxes to be an inherently governmental function,<sup>9</sup> and have never certified the type of work being performed by the private collectors as commercial.<sup>10</sup>*

The underlying premise of the PDC initiative is that certain tax collection activities are not inherently governmental—that simply asking the taxpayer to pay the tax in full, or over a relatively short period, does not involve the exercise of judgment or discretion.

Since the implementation of the PDC initiative, this premise has been roundly disproved. There are few “easy” tax collection cases—in fact, the designation of certain cases as “easy” itself reflects an IRS-centric view of the cases, as opposed to a taxpayer-centric view. No taxpayer views his or her tax collection case as easy, and it is because of the many questions and concerns these taxpayers raise during the resolution of their cases—even if they take a short amount of time to resolve—and the impact of those questions and concerns on the taxpayers’ continuing tax compliance that IRS employees should be the ones to interact with the taxpayer.

Taxes are fundamentally different from other types of debt owed to the Federal Government for several reasons. First, unlike other Federal obligations, taxes are the “lifeblood” of the government.<sup>11</sup> Second, because our tax system relies on the willingness of taxpayers to voluntarily report, file, and pay their taxes, there is the potential for an erosion of that willingness if taxpayers believe that the government or its contractors are acting capriciously in collecting the tax. Third, the correct tax liability often cannot be determined from the “four corners” of the taxpayer’s own return or even an IRS notice. Thus, taxpayers are allowed to dispute the correctness of a tax assessment, including their *own* original assessment on a return. These qualitative differences between tax debts and other government accounts militate against contracting out the collection of Federal tax debt.

## II. The Business Case for the PDC Program Is So Weak that the Program May Actually Lose Money.

The government has advanced several rationales and justifications for its use of private debt collectors to collect Federal taxes, including:

- Use of private collectors is a cost efficient and effective method to collect receivables that the IRS could not otherwise reach with its existing resources;<sup>12</sup>
- Private collectors will work the “easy” cases, thereby ensuring that they will not engage in “inherently governmental” activities and that the IRS will be able to focus on more complex work;<sup>13</sup> and
- Other Federal agencies have successfully used PCAs.<sup>14</sup>

Moreover, the IRS assured Congress that taxpayer protections would be “woven” throughout the program, “that PCAs would be prohibited from threatening or intimidating taxpayers,” and that “the PCAs would be governed by all of the same rules by which IRS employees are held accountable.”<sup>15</sup>

### A. The Amount of Revenue the PDC Program Is Projected to Raise Is Minimal.

The IRS projects the initial phases of the initiative (Release 1.1 and Release 1.2) will cost \$78 million and will bring in approximately \$134 million in gross revenue through FY 2008.<sup>16</sup> The IRS is using 43 of its own employees to monitor 81 of the PCAs’ employees.<sup>17</sup> From September 2006 through April 19, 2007, the PCAs have collected \$19.5 million in gross revenue. Of that gross revenue, only \$15.5 million was paid in response to a PCA contact. *\$4.0 million—or about 20 percent of gross*

<sup>9</sup> OMB Circular A-76 sets forth the standards under which Federal work is subject to competitive sourcing. As it existed in 1999, the collection of taxes was specifically listed as an inherently governmental function. In 2003, OMB Circular A-76 was revised to remove all specific examples of inherently governmental functions; see also General Accounting Office, IRS: Issues Affecting IRS’s Private Debt Collection Pilot (Jul. 18, 1997) (indicating that the IRS and the Department of the Treasury have long considered the collection of taxes to be an inherently governmental function).

<sup>10</sup> Internal Revenue Service FAIR Act certifications, available at <http://www.treas.gov/offices/management/dcfo/procurement/fair/inventories/index.html>.

<sup>11</sup> *Bull v. United States*, 295 U.S. 247, 259 (1935).

<sup>12</sup> Private Debt Collection: Hearing Before the Subcomm. on Oversight, House Comm. on Ways and Means, 108th Cong., 1st Sess. (May 13, 2003) (statement of Mark W. Everson, Commissioner of Internal Revenue).

<sup>13</sup> *Id.*

<sup>14</sup> *Id.*

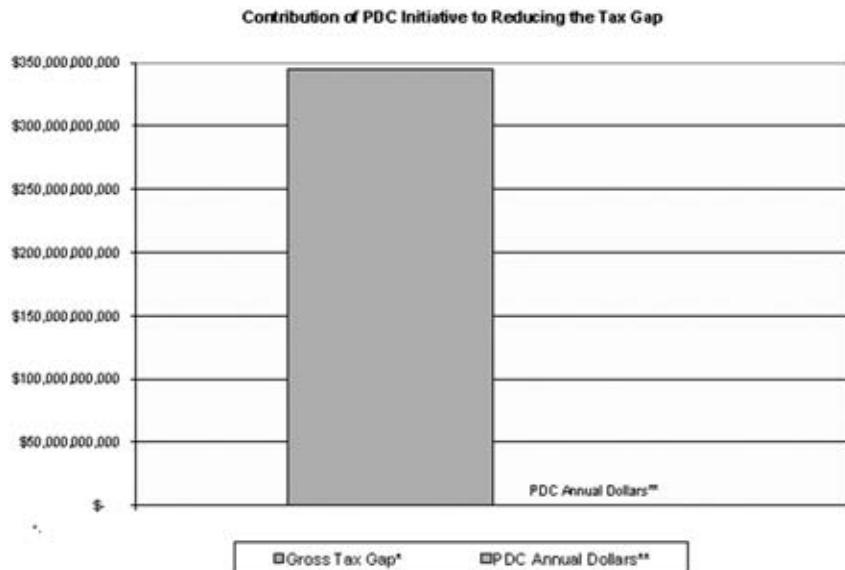
<sup>15</sup> *Id.*

<sup>16</sup> Internal Revenue Service, Filing and Payment Compliance Advisory Council (May 1, 2007) at 15.

<sup>17</sup> Data furnished by the IRS Filing and Payment Compliance Modernization Project Office (May 2007).

revenue—was collected by the IRS directly for only the cost of a stamp. Commissions actually paid on this \$15.5 million further limit the PCAs contribution to reducing the tax gap by another \$3.4 million, down to \$12.1 million.<sup>18</sup>

The IRS projects that the PDC initiative will bring in between \$1.5 and \$2.2 billion in gross revenue (before commissions) over ten years.<sup>19</sup> The midpoint of that ten-year range is \$1.85 billion, which translates to an average of \$185 million a year on a gross basis (before commissions and IRS administrative costs). Here is how the gross annualized PDC revenue stacks up to the IRS's most recent annual estimate of the gross tax gap:<sup>20</sup>



**B. The Opportunity Cost of Funding the PDC Program Instead of Hiring More IRS Collection Personnel Is Enormous, Resulting in a Significant Net Revenue Loss to the Treasury.**

The IRS estimates that it will spend about \$71 million in startup and ongoing maintenance costs through FY 2007.<sup>21</sup> If we applied this \$71 million and allocated it to the IRS Automated Collection System (ACS), we estimate that these funds would bring in about \$1.4 billion, as compared to the \$19.5 million brought in by the PDC initiative to date.<sup>22</sup>

This translates to a return-on-investment on the average ACS employee of about 20:1. The total dollars collected by ACS reflects the collections of both fully trained and new employees who underwent training during the year. The return is generally higher for trained employees and lower for newly hired employees. If the IRS were to hire 942 new employees, the return would predictably be lower than 20:1 during the initial training period. On the other hand, the amount of appropriated

<sup>18</sup> Internal Revenue Service, Private Debt Collection (PDC) Performance Update—Briefing for House Ways and Means Committee (May 18, 2007).

<sup>19</sup> Internal Revenue Service, Filing and Payment Compliance Advisory Council (May 1, 2007) at 14.

<sup>20</sup> The most recent IRS estimate of the gross tax was \$345 billion and was made in 2001.

<sup>21</sup> Internal Revenue Service, Filing and Payment Compliance Advisory Council (May 1, 2007) at 15. These estimated costs include startup and ongoing maintenance from the PDC Project Office, oversight, administration, and IT costs from FY 04 projected through FY 07. These estimated costs do not include infrastructure assessments for any MITS costs or costs associated with the TAS oversight or casework arising from the PDC initiative.

<sup>22</sup> The dollars spent on the PDC initiative could instead have been used to fund new ACS employees. We computed the fully loaded cost of an average ACS employee at about \$75,000 (assuming GS-8, step 5). A new employee would cost somewhat less. Based on IRS expenditures of \$71 million, the number of new ACS employees that could have been funded by the PDC initiative (about 942) was multiplied by the current average dollars collected by an ACS employee per year (about \$1.49 million) to estimate the revenue that could have been garnered by ACS in one year.

funds the IRS has spent on the PDC program to date has been greater than \$71 million because infrastructure costs and certain indirect costs (e.g., the full costs TAS has incurred) have not been included. If infrastructure and all related costs were included and also applied to fund additional ACS collection personnel, the number of employees the IRS could hire would be considerably greater than 942, resulting in higher potential revenue collections.

The IRS contends that the costs it is incurring to administer the PDC program will decline in the future. Even if the costs decline dramatically, the IRS still likely would be better off spending the funds on hiring more IRS collection personnel. In FY 2008, the IRS estimates that program, business project, contractor, and MITS costs will be \$7.35 million.<sup>23</sup> If we instead applied that \$7.35 million to ACS, the IRS would collect about \$146 million. By comparison, the IRS projects that the PCA initiative will bring in \$88 million in gross revenue in FY 2008. Thus, if the IRS applied its actual costs of program maintenance and supervision to ACS instead of the PCA initiative, the public fisc would be ahead by \$58 million for one year.

However, I am not persuaded that oversight costs or infrastructure costs for this initiative will decrease over time. First, so many program processes are manual that it will probably take ten years to achieve a truly automated system. Second, as discussed below, because there are no easy cases to send out to the PCAs, the IRS will have to reprogram its case assignment standards frequently to allow for cases under ever-expanding criteria. Third, based on experience to date, we will have periodic turnover of PCAs—we have already ended our contract with one of the three original agencies—and I suspect we would periodically be bringing one agency on and taking another off-line. Finally, as the Joint Committee on Taxation noted:

The use of private debt collectors may free up IRS resources to focus on other taxpayer delinquencies, thereby increasing total collections. On the other hand, the use of private debt collectors also raises concerns about the ability of the IRS to properly supervise these contractors and protect taxpayer privacy. The IRS has a finite amount of resources to devote to contractor supervision. As the number of private debt collectors increases, the ability of the IRS to closely supervise those collectors and ensure that the collectors are using appropriate safeguards and computer security decreases. As a result, the potential for abuse of taxpayer return information could increase.<sup>24</sup>

#### C. The IRS Embarked on the PDC Program without Undertaking Adequate Studies on the Cost Efficiency of the Program

To date the IRS has not conducted an adequate analysis of the return on investment of the PCA initiative, nor has it developed an adequate method of comparing the cost of PCA collection to the cost of IRS collection. My office is attempting to work with the Small Business/Self-Employed Operating Division to develop just such a test. Moreover, the IRS is currently not collecting the necessary data to truly understand the direct and downstream costs of this initiative. For example, the IRS now projects that 24 Full Time Equivalents (FTEs)—consisting of a total of approximately 43 employees—will work on the PCA initiative for FY 2007. However, this number does not include TAS employees working on PDC implementation or taxpayer cases, or Modernization & Information Technology Services (MITS) employees working on infrastructure improvements and routine servicing, or finance employees—much less IRS personnel responding to general phone calls to IRS toll-free numbers or contacts through the Taxpayer Assistance Centers.<sup>25</sup> Thus, the current employee and FTE counts are fluid and are not being tracked well. To get a better handle on the total FTE working on this initiative agency-wide, we are recommending that the IRS track PCA initiative time in the same manner that EITC initiative time is tracked, including separate time-keeping codes for all components of the IRS.

The IRS is currently attempting to design a test that will compare the cost of the PCA initiative with the cost of (a) ACS employees' working three types of the "next best case" per IRS analysis and (b) ACS employees' working cases from potential PCA inventory.<sup>26</sup> I have recommended that a true comparison of PCA effectiveness to IRS effectiveness would entail using IRS employees with limited authority similar

<sup>23</sup> Internal Revenue Service, Filing and Payment Compliance Advisory Council (May 1, 2007) at 15. These estimated costs exclude all infrastructure assessments.

<sup>24</sup> Joint Committee on Taxation, Present Law and Background Relating to Permitting Private Sector Debt Collection Companies to Collect Tax Debts, JCX-49-03 (May 12, 2003) at 5-6.

<sup>25</sup> The IRS's information technology office (MITS) identified 101 FTEs as devoted to the PDC initiative, attributable to start-up costs incurred now as part of Release 1.2, MITS Filing and Payment Compliance Release 1.2, Transition Management Plan, dated Nov. 22, 2006.

<sup>26</sup> IRS Filing & Payment Compliance, Private Debt Collection Cost Effectiveness Briefing (Feb. 20, 2007).

to the PCA employees to work PCA inventory. This test would involve the use of alternate databases and the Internet to locate current taxpayer addresses and phone numbers and would involve outbound calling. The IRS maintains that it would not work PCA inventory if it had funds to work additional cases. Unfortunately, the IRS has not conducted the necessary analysis to determine whether it would be more profitable to work these lower dollar cases earlier in the process, thereby eliminating many cases that are now worked in later years when they have grown much larger and complex.<sup>27</sup>

III. Despite IRS Representations to the Contrary, There Is No Such Thing as an “Easy” Tax Collection Case, and Even by the IRS’s Standards, There Are Far Fewer Such Cases than Originally Thought.

*“The cases the IRS would refer to PCAs are those where the taxpayer would likely pay the outstanding tax liability if contacted by telephone.”<sup>28</sup>*

Proponents of the PCA initiative have consistently stated that the IRS has a significant number of accounts in which taxpayers could be induced into paying what they owe by a simple phone call.<sup>29</sup> In fact, the assigned inventory turned out to be far more complex than the IRS ever expected. In the first batch of inventory identified for possible assignment to private collectors, for example, there was a high incidence of shelved delinquent tax return investigations.<sup>30</sup> Under the IRS’s traditional collection practices as well as the PDC-required procedures, taxpayers cannot obtain installment agreements if they are not compliant for other tax years, *i.e.*, they have not paid taxes or filed returns.<sup>31</sup> While the IRS plans to include this more complicated type of case in Release 1.2 when its systems can communicate the existence of the delinquent return to the private collector assigned to the account, it did not anticipate that such cases would be among the “simple” Release 1.1 inventory. In two different statistical samplings of the Release 1.1 inventory, the IRS learned that in over 30 percent of the cases there were unresolved delinquent tax return investigations in the taxpayers’ filing histories.<sup>32</sup> Thus, the IRS removed 15,500 cases from the initial 42,800 to be assigned to the collectors and used other inventory, including older cases, to make up for the deficit.<sup>33</sup>

The IRS also had to substitute older inventory when it identified two other unexpected case characteristics. In July 2006, the IRS eliminated another 10,000 cases from the potential inventory because payments on those accounts, which were thought to be voluntary, turned out to be involuntary levy payments.<sup>34</sup> Additionally, the IRS learned that its systems could not transfer updated account information identifying taxpayers as being represented by tax professionals. When the taxpayer files Form 2848, *Power of Attorney*, with the IRS, the IRS and private collectors under this initiative must contact the taxpayer only through the authorized representative. Consequently, it removed from inventory 5,500 accounts that were intended for assignment to private collectors.<sup>35</sup> *Thus, as of this date, taxpayers who have the resources to have obtained representation are exempt from this initiative.* Or stated another way, taxpayers who are unrepresented and vulnerable are disproportionately likely to be contacted by PCAs.

TAS ran its own comparison of the Adjusted Gross Income (AGI) levels of taxpayers whose cases were assigned to a PCA and taxpayers whose cases were assigned to IRS collection personnel. The median income of taxpayers whose cases

<sup>27</sup> For an in-depth analysis of current IRS collection strategy and recommendations for improvement, see National Taxpayer Advocate 2006 Annual Report to Congress at 80–82.

<sup>28</sup> Private Debt Collection: Hearing Before the Subcomm. on Oversight, House Comm. on Ways and Means, 108th Cong., 1st Sess. (May 13, 2003) (statement of Mark W. Everson, Commissioner of Internal Revenue).

<sup>29</sup> See Department of the Treasury, General Explanation of the Administration’s Fiscal Year 2004 Revenue Proposals 99 (February 2003), stating:

<sup>30</sup> A shelved delinquent tax return investigation is an investigation of a taxpayer’s failure to file a tax return for one or more years that have been closed as unresolved.

<sup>31</sup> See IRM 5.14.1 (July 2005); and IRS Private Collection Agency Policies and Procedures Guide (Sept. 2006) at 31.

<sup>32</sup> Internal Revenue Service, Partial Production Log (March 16, 2006).

<sup>33</sup> Internal Revenue Service, Filing & Payment Compliance Advisory Council Presentation (Jul. 31, 2006) at 9.

<sup>34</sup> The initial criteria for assignable inventory in Release 1.1 limited inventory to cases where the taxpayer indicated the amount is due on a tax return and cases where the tax has been assessed and the taxpayer has made three or more voluntary payments on the tax. Private Debt Collection: Hearing Before the Subcomm. on Oversight, House Comm. on Ways and Means, 108th Cong., 1st Sess. (May 13, 2003) (statement of Mark W. Everson, Commissioner of Internal Revenue).

<sup>35</sup> Internal Revenue Service, Filing & Payment Compliance Advisory Council Presentation (Jul. 31, 2006) at 9.

were assigned to a PCA was significantly less than the median income of taxpayers whose cases were assigned to IRS collection personnel. Moreover, 23 percent of the PCA taxpayer population is projected to receive the Earned Income Tax Credit (EITC) as compared to 19 percent of the total IRS collection population.<sup>36</sup> These findings heighten concerns that lower income taxpayers are disproportionately represented in PCA case assignments.<sup>37</sup>

**A. The Absence of “Easy” Cases Has Forced the IRS to Outsource “Harder” Cases, Which Will Prove Harder to Collect on.**

The shortage of the promised “easy” inventory is driving the IRS to assign inventory with the types of complexities that were never intended to be worked by private collectors. As described above, the IRS plans to assign accounts known to be non-filers in Release 1.2. Utilizing private collectors to interact with taxpayers about their obligation to file tax returns raises multiple problems, including the lack of training of private collection employees as to which taxpayers are required to file tax returns. Depending on the taxpayers’ circumstances, they may be under no legal obligation to file tax returns.<sup>38</sup> Private collectors have not been trained to determine when filing is required and when it is not. In fact, since such a determination requires the exercise of judgment and discretion, the authority to make a determination of a filing requirement *cannot* be delegated to a non-governmental employee.

But the case criteria expansion does not stop there. The IRS says that it has 132,000 case modules available that meet “primary” inventory criteria, which are enough to meet the anticipated case assignments through January or February 2008. In order to send out the necessary cases for the remainder of FY 2008 and into FY 2009, the IRS is looking at a pool of over 690,000 cases “that do not meet primary placement criteria that could be assigned without additional programming and another 383,000 that have been identified if additional programming was performed.”<sup>39</sup> Moreover, the IRS states that “programming must begin within the next few months so that enough inventory is available for the future.”<sup>40</sup>

I am concerned about the use of the phrase “primary placement criteria” in the IRS’s analysis above. This phrase implies that Congress understood that IRS intended all along to expand the inventory criteria from those “easy” cases that only required a phone call to resolve, into older cases, nonfiler cases, or U.S. territory and possessions cases. Yet we can find no public document or discussion of this expansion, either in the initial 2003 congressional hearings or in the legislative history. The Joint Committee on Taxation described the Administration’s budget proposal as follows:

The proposal generally applies to any type of tax imposed under the Internal Revenue Code. The Treasury anticipates that the focus in implementing the proposal will be: (a) taxpayers who have filed a return showing a balance due but who have failed to pay that balance in full; and (b) taxpayers who have been assessed additional tax by the IRS and who have made several voluntary payments toward satisfying their obligation but have not paid in full. The Treasury anticipates that the IRS will commence implementation of the proposal with debts owed by individuals.<sup>41</sup>

In Appendix D, we describe the cases that the IRS plans to send, or is considering sending, to the PCAs in order to meet IRS revenue projections for the project. Of these expanded categories, we are particularly concerned about the potential assignment of Automated Collection System (ACS) cases. These are cases in which the IRS has already made some sort of determination that a case has the potential for enforcement activity and therefore is in the queue for assignment to an IRS ACS employee. Despite former Commissioner Everson’s explicit assurances to the Ways and Means Oversight Subcommittee that “[t]he IRS would not refer to PCAs cases for

<sup>36</sup> IRS Compliance Data Warehouse, Accounts Receivable Dollar Inventory (ARDI) (CY 2007, first quarter) and Individual Returns Transaction File (TY 2005).

<sup>37</sup> Among cases scheduled for assignment to a PCA during the first quarter of FY 2007 and also having a Tax Year 2005 return filed (based on match of primary SSN), median adjusted gross income was \$24,000, while median adjusted gross income was \$31,565 among cases not scheduled for assignment to a PCA. It should be noted that only 36 percent of PCA cases and 56 percent of non-PCA cases showed the filing of a Tax Year 2005 Individual Income Tax Return.

<sup>38</sup> See IRS Publication 501, Exemptions, Standard Deduction and Filing Information; IRS Publication 17, Your Federal Income Tax for Individuals.

<sup>39</sup> Internal Revenue Service, Filing and Payment Compliance Advisory Council Deck (May 1, 2007) at 9.

<sup>40</sup> Internal Revenue Service, Filing and Payment Compliance Advisory Council Deck (May 1, 2007) at 11.

<sup>41</sup> Joint Committee on Taxation, Present Law and Background Relating to Permitting Private Sector Debt Collection Companies to Collect Tax Debts, JCX-49-03 (May 12, 2003).

which there is any indication that enforcement action would be required to collect the tax liabilities,<sup>42</sup> the IRS is now anticipating that it must send out these cases to meet the revenue targets it has established for the program.

In fact, the IRS acknowledges that it will run out of inventory sometime in February 2008 unless it expands the criteria for cases. Thus, the IRS plans to accelerate a test on certain extremely low-dollar cases because if it waits too long to assign these low-dollar cases to the PCAs, “[p]rojections would not be met due to low average balance due.”<sup>43</sup> Moreover, the IRS notes that *[n]ot expanding inventory [beyond primary criterial] would lead to a large number of lower dollar deferred cases being placed with the PCAs, which would significantly reduce PCA collections.*<sup>44</sup> Thus, the IRS appears to be more concerned about “smoothing revenue” to make the program look like a success than it is with either acknowledging that its projections will not be met—namely, that IRS doesn’t have the “easy” cases it originally believed it had—or considering the impact such referrals may have on taxpayers.

#### B. Expanding Case Referral Criteria Poses Threats to the Integrity and Fairness of Tax Collection.

Expanding the inventory beyond the primary criteria—to ACS cases, to cases involving U.S. territories and possessions, to business taxes, to nonfilers, and to older cases—increases the likelihood that the PCAs will make mistakes and decreases the likelihood that the PCAs will actually be able to collect any payment from the taxpayer. As the Joint Committee on Taxation noted in its analysis of the proposal in 2003:

Another issue is the extent to which taxpayers will voluntarily pay the amounts owed in response to the private debt collectors or will raise procedural or substantive issues that will require referral of their cases back to the IRS. It is possible that such referrals back to the IRS may consume considerable resources of the IRS.<sup>45</sup>

In these complex cases, taxpayers are more likely to have questions that the PCA employees are unable to answer because their knowledge regarding tax issues is limited, at best, or because the PCAs cannot exercise discretion in either answering a question or working a case. First, as the expanded case selection increases the likelihood of IRS Referral Unit involvement, the underlying business case for the PCA initiative evaporates. Second, and more important from the taxpayer’s perspective, faced with having to send the case back to the IRS Referral Unit, the PCAs may attempt to pressure the taxpayer into a payment plan. Here are a few case examples where the PCA continued pressuring the taxpayer into paying rather than answering the taxpayer’s question or making a referral to the IRS Referral Unit.

**Case One:** A taxpayer called a PCA to try to work out a payment arrangement. The taxpayer asked whether some of the interest charges could be abated. Interest abatement requires the exercise of discretion and can only be evaluated by an IRS employee, but the PCA did not offer to refer the case to the IRS on that basis. In addition, the taxpayer said she could not afford the \$793 per month in payments the PCA was requesting over a four-month period. Initially, the taxpayer was not offered any payment plan longer than 120 days despite the fact that taxpayers are allowed to enter into installment agreements of up to 36 months under the existing PCA guidelines. The taxpayer asked to speak with TAS. The PCA employee and a supervisor told the taxpayer that TAS’s role is not to set up payment agreements but to assist with situations such as significant hardship. Eventually, the PCA supervisor offered to work out a payment arrangement of less than \$793 per month. However, the taxpayer was frustrated by that point and insisted on working with TAS.<sup>46</sup>

**Case Two:** During the initial phone call, the taxpayer indicated she did not owe the tax because the apparent liability resulted from a mistake by her tax preparer.

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<sup>42</sup> Private Debt Collection: Hearing Before the Subcomm. on Oversight, House Comm. on Ways and Means, 108th Cong., 1st Sess. (May 13, 2003) (statement of Mark W. Everson, Commissioner of Internal Revenue).

<sup>43</sup> Internal Revenue Service, Filing & Payment Compliance Advisory Council (May 1, 2007) at 12. These are “Status 23 Deferred” cases where the amount of the liability is below tolerance—i.e., the dollar amount is so small that it is just not worth it for the IRS to collect. According to the IRS, there are 595,065 existing Status 23 Deferred cases, with an extremely low average balance due. *Id.* at 10.

<sup>44</sup> Internal Revenue Service, Filing & Payment Compliance Advisory Council (May 1, 2007) at 24.

<sup>45</sup> Joint Committee on Taxation, *Present Law and Background Relating to Permitting Private Sector Debt Collection Companies to Collect Tax Debts*, JCX-49-03 (May 12, 2003) at 6 (citations omitted).

<sup>46</sup> Contractor Officer Technical Representative (COTR) case review write-up; Taxpayer Advocate Management Information System (TAMIS).

The taxpayer was trying to get a portion of the funds submitted with a joint extension of time to file credited to her married filing separately account. The PCA placed several temporary holds on collection activity, but when the case was referred to TAS, almost four months after the taxpayer's initial conversation with the PCA, the PCA was still making outbound calls to attempt to collect the tax. These calls occurred notwithstanding that on several occasions during this timeframe, the taxpayer submitted a letter outlining her dispute.<sup>47</sup>

These two examples illustrate how difficult it is to identify "easy" cases. These examples also demonstrate that complex cases increase the likelihood that when PCA employees don't know how to or can't respond to taxpayers' questions, they simply continue trying to collect the tax.

**IV. Whereas the IRS Attempts to Provide Service to Taxpayers, PCAs Are Compensated Primarily Based on Revenue Collection and Have Little Incentive or Ability to Assist Taxpayers Who Have Special Needs, Who May Not Owe the Alleged Tax Liability, or Who May Lack the Ability to Pay.**

PCAs are given very little training about tax law or procedure, are not permitted to enter into discussions with taxpayers about matters that require the exercise of discretion (e.g., to compromise a tax debt or abate interest or penalties), and have no economic incentive to do more than collect the maximum number of dollars as quickly as possible. While IRS employees are far from perfect, they receive broader instruction about tax law and procedure, have the authority to exercise discretion, and seek to foster maximize long-term compliance. The differences in how taxpayers are treated and assisted will predictably be significant.

**A. PCAs Are Unable to Meet the Diverse and Complex Needs of Taxpayers.**

Taxpayers have a variety of diverse and complex needs and deserve to interact with an organization that can meet those needs. However, providing quality customer service seems to be superseded by the PCAs' motivation to secure payment from the taxpayer and collect their commission. This motivation is made clear by the three contractors' operational plans for the first phase of the PCA initiative, which place a heavy emphasis on collection results rather than customer service. The IRS, on the other hand, devotes significant resources specifically toward meeting the needs of taxpayers.

The IRS Multilingual Initiative (MLI) is one example of the IRS making an effort to address taxpayers' needs. IRS started this initiative to address the needs of taxpayers who have Limited English Proficiency (LEP).<sup>48</sup> The PCAs, however, have made little to no effort to address LEP or other issues relating to taxpayer populations with special needs, and it is highly unlikely that PCAs can or will duplicate this type of initiative. In fact, only one PCA has a telephone number for Spanish speaking taxpayers, and the other PCAs provide virtually no LEP services. Further, when TAS representatives dialed the one PCA's Spanish-speaking number, there was only an English-speaking voice, which transferred the call to another line; the call was then automatically terminated. The PCA has apparently corrected the problem, but the fact that TAS discovered this failure demonstrates the low priority PCAs place on taxpayer service.

The IRS acknowledges these problems in PCA taxpayer service delivery and has asked TAS to handle multilingual taxpayer cases until the PCAs have developed the resources to work these cases. TAS has agreed to do so, but this situation raises several serious concerns. First, the IRS should have ensured that PCAs could meet the needs of all taxpayers prior to awarding contracts. Second, there is no determination on when or how the PCAs will develop these resources. Third, TAS picking up these cases and working them demonstrates that even apparently "easy" cases are not easy, results in IRS employees' working cases that they weren't planning to work, and increases the opportunity cost of the PDC initiative by pulling TAS employees off presumably more productive cases to work these cases.

**B. PCAs Utilize Psychological Techniques to Collect the Maximum Amount from Taxpayers.**

Throughout the fall of 2006, TAS representatives reviewed the three PCAs' operational plans and made numerous requests for changes. One such objection involved a PCA collection script placed in one of the private collectors' operational plans which required representatives to advise taxpayers "Your balance of \$\_\_\_\_\_ is due in full today." followed by the question "How can we help you resolve this?" The

<sup>47</sup> IRS Private Collection Agency Complaint Review Panel.

<sup>48</sup> Internal Revenue Service, Multilingual Initiative Customer Base Report FY 2006 (Feb. 2006) at 12.

script then requires the collection representative to employ a “*Psychological pause—let the Taxpayer speak first*,” (emphasis in original), in which the representative says nothing and waits for the taxpayer to commit to a payment amount. After the taxpayer provides a commitment or financial information, the collector responds “*GREAT . . . Before we continue, Federal law requires me to inform you that this is an attempt to collect a debt, any information obtained will be used for that purpose.*”<sup>49</sup> (Emphasis in original.)

TAS objected to the entire script. TAS has not been permitted to interact directly with the PCAs and must communicate through the IRS representatives. In response to TAS’s objection, the IRS asked the PCA to remove the word “psychological” from the phrase “psychological pause.” TAS representatives informed the IRS that this was an insufficient remedy because the Fair Debt Collection Practices Act (FDCPA) warning still came after the taxpayer volunteered information. Additionally, because private collectors had already been operating under the script for months, we asked that the employees be given some type of instruction clarifying the correct approach. The IRS did not respond to those additional TAS requests. In response to the discussion of this issue in the National Taxpayer Advocate’s 2006 Annual Report to Congress, the PCA in question revised its script to provide its FDCPA warning at the beginning of the conversation; however, the PCA still uses the “pause” as a device.<sup>50</sup>

Since publishing the 2006 Annual Report to Congress, we have learned that the other two PCAs also employ this and other disturbing devices.

#### Training Materials for Linebarger Goggan:<sup>51</sup>

##### Training Plan:

“Use the psychological pause (pregnant pause):

Once you ask for payment in full, pause for the taxpayer’s response. *Silence will work in your favor.*” (Emphasis added.)

##### Sample Phone Script:

Collection Representative: “What are your intentions regarding payment on your account?”

Psychological Pause:

*The next person to speak loses.* (Emphasis added.)

#### Training Materials for CBE:<sup>52</sup>

We have found the following references in PCA training materials and scripts. We have not looked into the collection practices used by other Federal agencies. The IRS is subject to an entirely different set of laws, regulations, and procedures from other Federal agencies, reflecting its unique role as the Federal tax system’s administrator and enforcer. Congress’ concerns over past IRS practices, including collection practices, have led to enactment of three Taxpayer Bills of Rights, with numerous protections for taxpayers. While we have not expressed an opinion that these tech-

<sup>49</sup> Pioneer Credit Recovery, Inc., “The Initial Demand.” A copy of this script is attached as Appendix A.

<sup>50</sup> See National Taxpayer Advocate 2006 Annual Report to Congress at 60. While we were preparing the 2006 Annual Report to Congress, the IRS advised us that the operational plans and calling scripts of the PCAs were proprietary and therefore generally could not be released without the PCAs’ consent. We found this disturbing because one of the principles on which the PDC initiative was predicated was the existence of a “level playing field,” meaning that rules and restrictions applicable to the IRS and its employees would apply equally to PCAs and their employees. The collection procedures followed by IRS personnel are published in the Internal Revenue Manual, so the “proprietary” designation of PCA operational plans and calling scripts violates the “level playing field” principle. After we raised concerns, the IRS asked the PCAs for consent to disclose the scripts. The responses were mixed. After our report was issued, two PCAs provided consents. The third PCA, Pioneer, offered to give consent only if the IRS agreed not to require PCA employees to refer cases to TAS immediately if the taxpayer makes such a request. TAS opposed this condition, and the IRS made clear that callers who asked to be referred to TAS must be so referred. We were informed on February 27, 2007, that Pioneer finally gave an unconditional consent.

<sup>51</sup> The referenced section of the Resource Guide is attached to this document as Appendix B.

<sup>52</sup> The referenced section of the Resource Guide is attached to this document as Appendix C.

protections for taxpayers. While we have not expressed an opinion that these techniques violate any laws, we do believe that these techniques are inconsistent with the values built into IRS customer service initiatives since the IRS Restructuring and Reform Act of 1998. Were a taxpayer to complain to the National Taxpayer Advocate about such a script being used by IRS employees, I would immediately demand that the script be changed and that remedial training be offered to all collection employees, and I would refer the specific case to the Treasury Inspector General for Tax Administration (TIGTA) for investigation of potential intimidation. I would react the same way were I to see IRS training materials utilizing "Glengarry Glen Ross" type selling techniques (e.g., "close the sale").

My concerns about these techniques arise in part from my experiences in my former practice, which are confirmed by reports from Low Income Taxpayer Clinics (LITCs). I represented low income taxpayers for many years in states that retained private debt collectors for the bulk of their tax collection activity. I found that taxpayers routinely agreed to installment agreements with monthly payment amounts greatly in excess of what they could afford and often at harm to their welfare and their ability to be compliant in the future. They offered up any amount in order to be free of the collection agency and did not ask about lower amounts for fear of what the collection agency might do. Needless to say, taxpayers frequently defaulted on these agreements and ended up in my clinic's office for assistance.

Agreeing to an unreasonable installment agreement that will result in a default is not neutral to the IRS or the taxpayer. From the IRS perspective, this taxpayer has demonstrated additional noncompliance and will require additional (costly) contacts and efforts, including levies. The taxpayer no longer qualifies for a guaranteed installment agreement<sup>53</sup> and will have to submit additional financial information (and pay an additional user fee) to reinstate the installment agreement or enter into a new one.<sup>54</sup> If the taxpayer attempts to enter into an offer in compromise, his defaulted installment agreement may count against him.<sup>55</sup> From the taxpayer's perspective, he now may be even more uneasy or afraid about communicating with the IRS, in addition to having fewer options, potentially reducing the taxpayer's future compliance. All of this could be avoided were taxes collected the right way—*i.e.*, with an eye to future compliance and the particular circumstances of the taxpayer. The "psychological pause" instructions and attendant consequences demonstrate an important difference between the compliance-oriented IRS and the profit-oriented PCAs.

I do not know whether the "psychological pause" practice violates the FDCPA. I do know that it harms taxpayers, does not contribute to future compliance, and may very well constitute intimidation in certain cases. In certain instances, this practice might violate § 1203 of the IRS Restructuring and Reform Act of 1998. It is certainly an example of the kind of behavior Congress sought to change through three Taxpayer Bills of Rights. Such an approach is an example of the profit-motivated approach of the PCAs, and does not constitute taxpayer service within enforcement. It is not the right way to collect tax, which should take into consideration not only the need to hold taxpayers accountable but also the specific facts of their cases, including their financial circumstances.<sup>56</sup>

#### C. The PDC Procedure for Authenticating the Identity of a Taxpayer Is Off-putting and Frightening to Some Taxpayers.

When an IRS collection employee contacts a taxpayer, he is permitted to say that he is calling from the IRS. That information alone is generally sufficient to let the taxpayer know the nature of the call. When a PCA contacts a taxpayer, however, the PCA employee is not permitted to identify the nature of the debt about which he is calling until after he verifies the identity of the taxpayer, typically by asking the taxpayer to provide his Social Security Number (SSN). In theory, a letter precedes the phone call. But if the letter didn't reach the taxpayer or the taxpayer didn't focus on it, the taxpayer will be taken aback upon receiving a call about a debt and being asked to provide his SSN, and some taxpayers understandably refuse to provide their SSNs to an unknown caller.

<sup>53</sup> IRC § 6159(c)(2)(C).

<sup>54</sup> IRM 5.14.11.7(2); IRM 5.19.1.5.4.3(1).

<sup>55</sup> For example, an offer-in-compromise based on effective tax administration can be rejected because of the taxpayer's compliance history. IRM 5.8.11.2.1(7).

<sup>56</sup> TAS recently learned that IRS assigns accounts involving innocent spouse relief, the ten percent IRA early withdrawal penalty, and the trust fund recovery penalty to PCAs if the PCA already has a case involving that taxpayer. One can only imagine how an innocent spouse who is a victim of domestic violence or a struggling small business owner would respond to a "psychological pause" technique.

Indeed, one of the PCAs, CBE Group Inc. (CBE), when phoning taxpayers, simply states the call is in reference to a business matter, even though they are authorized to disclose the nature of their work, *i.e.*, debt collection, prior to authentication. This practice has resulted in CBE having a significantly higher number of complaints than the other PCAs. Specifically, to date there are 21 complaints about CBE's authentication process.

**D. PCAs Have Violated Procedures for Informing Taxpayers About Their Right to Opt Out of the Program and About TAS.**

Upon the request of a taxpayer, a PCA employee must allow that taxpayer to opt out of working with the PCA.<sup>57</sup> The drafts of letters from PCAs to taxpayers that have been provided to TAS do not contain language designed to inform taxpayers that they have the right to "opt out" of the PCA initiative. To our knowledge, the only document that contains this information is the IRS pamphlet, *What You Can Expect When the IRS Assigns Your Account to a PCA*, which is sent to taxpayers when the accounts are initially assigned to PCAs.

From the inception of this initiative, TAS has advocated for the right of taxpayers to come to TAS upon the request of the taxpayer as an additional protection for taxpayers. The PCA Policies and Procedures Guide includes instructions to the PCA employees that they must inform taxpayers about TAS and requires PCA employees to refer cases to TAS at the taxpayer's request. PCA employees are also required to inform taxpayers about the availability of LITCs. The Guide instructs PCA employees about how to identify potential TAS cases and make referrals to TAS without the taxpayer's request, just as IRS employees are required to do.<sup>58</sup>

Months after the initiative began, TAS learned that one of the PCAs was not adhering to the Guide's requirement that taxpayers must be referred to TAS upon request and instead was coaching its employees to continue to attempt account resolution even after the taxpayer requested to come to TAS. More recently, when the IRS was negotiating with this PCA over whether it would agree to make its scripts public, the PCA attempted to condition the release of its script on the IRS validating its practice of not referring taxpayers to TAS upon request. TAS rejected this condition.

Subsequently, we discovered that the practice was not isolated to one PCA. At least one other PCA was failing to refer taxpayers to TAS upon request and was not even providing the TAS phone number to taxpayers upon request unless the taxpayer stated he or she was experiencing a "severe hardship." Such a precondition for referral is contrary to the PCA Policies and Procedures Guide. The IRS subsequently issued an alert to all PCAs that this practice is violation of procedures.

**E. PCA Employees Receive Limited Training and Experience High Turnover.**

The number of PCA collectors who either were taken off the contract or are no longer employed at the PCA is disturbing. For example, over 50 percent of CBE's collectors have either been taken off the contract or are no longer employed by CBE.<sup>59</sup> In contrast, 77 percent of W&I and SB/SE customer service representatives have a year or more experience.<sup>60</sup> When the PCA collector position is a revolving door, it is unlikely that these employees adequately understand IRS cases. More importantly, it is highly unlikely that these employees will have engrained in them the special protections that adhere to U.S. taxpayers under the Internal Revenue laws. In contrast to IRS employees, who receive taxpayer rights and confidentiality training every year over the course of their long careers at the IRS, PCA employees only receive several hours of IRS training, of which taxpayer rights is a small component.<sup>61</sup>

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<sup>57</sup>The FDCPA, which is applicable to PCAs, requires debt collectors to cease communication efforts if the debtor makes this request in writing, 15 U.S.C.A. § 1692c(c); see also Private Debt Collection Agencies Policy and Procedures Guide, Section 12.14 (incorporating the FDCPA opt-out provision).

<sup>58</sup>TAS also produced video training, including a 20-minute presentation by the National Taxpayer Advocate and a two-hour discussion by TAS personnel, that is required to be taken by all PCA employees about TAS, taxpayer rights, LITCs, and procedures for referring TAS cases.

<sup>59</sup>Pioneer had a 20.8 percent turnover rate for collectors, CBE had a 52.8 percent turnover rate for collectors, and LBGS had a 25 percent turnover rate for collectors. (Calculation based on PCA list of "Collector" and "Collector/IRS Referral Unit" Liaison employees provided by the IRS PDC project office).

<sup>60</sup>Internal Revenue Service, Human Capital Office Workforce Plan, IV-53 (March 2006).

<sup>61</sup>IRS employees receive substantial, in-depth training before handling collection matters. For example, ACS employees receive mandatory training on unauthorized access, ethnic awareness, computer security, and annual Continuing Professional Education. In FY 2005, this training was a total of 24 hours and eight hours of localized training. In contrast, PCA employees receive

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#### V. TAS Cases Illustrate Some of the Problems Taxpayers Have Experienced.

As of May 21, 2007, TAS has received 318 cases relating to taxpayer concerns about the PCAs. These cases were received from the TAS Intake Line, as a referral from the PCA, or from IRS employees answering toll-free lines. Once TAS receives a case, the TAS Case Advocate identifies the issue that needs to be resolved and works with the taxpayer to resolve that issue. During the time that TAS is working with the taxpayer, the PCA must cease all collection activity. TAS has closed 242 of the 318 referred PCA cases. Appendix E provides an analysis of TAS cases received to date.

TAS monitors these cases in an effort to identify any trends that may have a negative impact on taxpayers. For example, TAS identified a situation where taxpayers assigned to a PCA were being treated differently from taxpayers with a similar situation dealing directly with the IRS. In this situation, the taxpayer was requesting an installment agreement with a term of more than three years but less than five years. The PCA employee cannot unilaterally enter into an installment agreement for over three years' duration and is required to refer that case to the IRS. The PCA taxpayer was required to submit a financial statement in this situation. However, if the case were being worked directly by the IRS, the taxpayer would have received a 60-month agreement without submitting a financial statement. TAS is currently working this issue with the PDC Project staff; *in the meantime, the PCA procedures continue to excessively burden taxpayers and allow the PCA access to taxpayer financial information that it has no reason to acquire.*

The following examples involve PCA cases where the taxpayer called TAS directly. They demonstrate the fallacy of the IRS's assertion that it is sending "easy" or "clean" cases to the PCAs and demonstrate why the IRS alone—with its full panoply of assessment, abatement, and collection authorities—should be working taxpayer-collection cases.

- The taxpayer called TAS after receiving a letter from a PCA. After sustaining injuries in a near-fatal automobile accident, the taxpayer is living off only Social Security benefits and food stamps and was unable to pay the balance due.
- The taxpayer incurred a balance due as a result of an early withdrawal from her retirement plan. The taxpayer is currently on Social Security disability income. She is also taking care of her ill mother and is unable to pay at this time.
- The taxpayer's debt arose from her 1998 tax return, on which the IRS disallowed the taxpayer's youngest child, born December 1, 1998, for purposes of the dependency exemption and EITC. The taxpayer sent proof of her child's birthday to the IRS on three separate occasions. The IRS told the taxpayer that the period of limitations for making changes to her tax return has expired, and it has offset additional refunds in the amount of \$2,000.
- The taxpayer's tax returns were examined for each of tax years 2001 through 2005, resulting in EITC disallowances. Each year, the taxpayer submitted all requested documents but did not receive a response. The taxpayer states that the claimed children are hers, and she does not understand why the claim on her return is continually being disallowed. She has called the IRS several times and cannot obtain assistance.
- The taxpayer stated that he has been receiving bills for taxes that he does not owe. The taxpayer has resided in Puerto Rico for his entire life. He has proof of filing with the Hacienda and says he has reported all his earned income.
- The taxpayer called TAS in response to a letter from a PCA. The taxpayer stated that he does not owe the tax debt. The taxpayer said he did not work for the tax year at issue and did not file a tax return for that year, nor did he receive a refund. He suspects his child's mother may have helped someone improperly use his information to file.

#### VI. The PCA Initiative Raises Concerns about the Confidentiality and Security of Taxpayer Information.

The Internal Revenue Code places significant emphasis on the confidentiality and security of taxpayer information. When taxpayer information is shared with outside contractors, the risks of misuse and the steps required to secure information both increase.

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minimal training on complex topics before handling collections matters. For example, PCA employees receive 20 minutes of training on privacy awareness, 20 minutes on disclosure and safe-guard awareness, 20 minutes on the Taxpayer Bill of Rights and Taxpayer Advocate Service, 20 minutes on § 1203 of the IRS Restructuring and Reform Act of 1998, and 20 minutes on the role of the Treasury Inspector General for Tax Administration. PCA employees also view a two-hour video produced by the Taxpayer Advocate Service. National Taxpayer Advocate's 2005 Annual Report to Congress at 85–86.

**A. The IRS Recently Terminated a PCA for Failing to Perform at Appropriate Standards, Yet the PCA Is Permitted to Retain Taxpayer Information for an Additional Two Years.**

As Linebarger's contract came to an abrupt end, new security concerns have arisen. The IRS is permitting a PCA, which is no longer part of the initiative, to keep and maintain taxpayers' files for two years after the contract has ended. Allowing PCAs to hold onto taxpayer information after a PCA has left the initiative is a failure of the IRS's fiduciary duty to protect taxpayer information and significantly compromises taxpayer information.<sup>62</sup> It is especially disturbing that Linebarger will keep taxpayer information for two years after the contract, since Linebarger's security breaches were a major focus of a recent TIGTA Report. Some of the concerns the report addresses include the following:

- Two storage rooms were not wired with alarm systems;
- Perimeter doors did not have sufficient locking mechanisms; and

It seems irresponsible and foolish to allow any PCA to keep taxpayer information for two years after contract expiration, but especially foolish to allow a PCA to keep taxpayer information where that PCA was significantly criticized for security breaches in a recent TIGTA report.

**B. PCAs Are Now Receiving Sufficient Information About Taxpayers to Enable Identity Theft.**

As described above, PCAs are required to verify that they are talking to the correct taxpayer before they can disclose the specific purpose for the phone call or discuss details of the account. Now, in addition to PCAs' having the taxpayer's name, last known address, and SSN, they also want the taxpayer's date of birth to make the authentication process easier. One wonders how comfortable taxpayers would feel knowing that the IRS is handing over more and more of their information to private collectors.

The rate at which collectors either are taken off the IRS contract or are no longer employed at the PCA is alarmingly high. For instance, Pioneer had a 20.8 percent turnover rate for collectors, CBE had a 52.8 percent turnover rate for collectors, and LBGS had a 25 percent turnover rate for collectors. In contrast, 77 percent of ACS employees have a year or more of experience.<sup>64</sup>

**VII. The IRS Can Do It Better**

As stated previously, a central tenet of the PDC initiative is that the IRS has a significant number of accounts in which taxpayers could be induced into paying what they owe by a simple phone call.<sup>65</sup> The mere fact that there is a substantial pool of cases that effectively result in revenue if only someone contacts the taxpayer does not mean that PCAs are the best qualified to handle these cases.

- Indeed, the IRS is clearly the superior collection agent for these cases: The IRS currently possesses a large collection infrastructure with thousands of trained employees and an annual budget of nearly two billion dollars.<sup>66</sup> The IRS has 14 ACS sites that interact with millions of taxpayers annually, in contrast to the private collectors who operate out of single locations with 81 employees in the aggregate.
- The IRS employs and continues to spend significant resources on the same technology used by private collectors, such as predictive dialer systems.<sup>67</sup>
- The IRS maintains and utilizes various internal and external databases for research purposes, including but not limited to Integrated Data Retrieval System, Choice Point, and the United States Postal Service. Many of these are the same

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<sup>62</sup> The IRS could store and maintain taxpayer files and allow the PCA access to the files in case of a civil suit.

Multiple PCA employees had keys to the IRS work area and one of these employees did not need access to Federal tax information.<sup>63</sup>

<sup>63</sup> Treasury Inspector General for Tax Administration, *The Private Debt Collection Program Was Effectively Developed and Implemented, but Some Follow-up Actions Are Still Necessary* (Mar. 27, 2007).

<sup>64</sup> Internal Revenue Service, Human Capital Office Workforce Plan, IV-53 (March 2006).

<sup>65</sup> See Department of the Treasury, General Explanation of the Administration's FY 2004 Revenue Proposals (Feb. 2003) at 99, stating:

<sup>66</sup> IRS FY Budget in Brief, available at: <http://www.irs.gov/pub/irs-utl/bib-irs.pdf>. Excluding operations support costs, the IRS's total budget for tax law enforcement in fiscal year 2006 was approximately \$4.7 billion dollars and its proposed enforcement budget for FY 2007 is approxi-

sources currently being utilized by the PCAs to attempt to locate and contact PDC-assigned taxpayers.

Furthermore, timely and personal interventions on collection accounts are powerful motivations for taxpayers to resolve tax problems and cannot be discounted. These interventions represent the appropriate point in the collection process to identify and resolve issues that have caused the taxpayers to become delinquent, thereby preventing future noncompliance, and to explore meaningful payment options. Many of the accounts currently being assigned to PCAs are less than \$25,000 and thus would qualify for guaranteed or streamlined installment agreements (IAs).<sup>68</sup> The IRS already has the means and proven track record to effectively handle these types of accounts.<sup>69</sup>

The IRS could collect taxes even more effectively if it were to enhance and refine its existing automation and technology. The predictive dialer system and the online research tools that the IRS maintains are both effective means of contacting and locating taxpayers, but neither is being utilized to its fullest capacity. For example, the predictive dialer system is predominantly used *after* all required notices are sent, a notice of levy issued, and there is no response from the taxpayer. If outbound contact were moved up in the notice stream and ACS process, the IRS could make even more timely and effective contacts and be more likely to reach resolution, without the need for enforcement action.

Similarly, the IRS also has a vast array of internal and external research sources at its disposal, including a sophisticated “skip tracer-like” mechanism—the Address Research System (ADR). While ADR has the potential to validate or update potential addresses for a given taxpayer, the IRS currently uses this resource selectively, usually late in the collection process. If the IRS were to expand its search tool to include such sources as the Internet, Department of Motor Vehicles records, and voting registries, and employ the search tool earlier in the collection process, it could improve the collection productivity of its existing personnel.

### VIII. Ultimately, Tax Collection Is the IRS's Responsibility.

IRS collection activities are compliance-based, and the training of its employees reflects that fact.<sup>[70]</sup> In other words, the collection policy followed by IRS collection representatives is to first cure the taxpayer's current noncompliance, whether through increased withholding or taking other actions, rather than seeking repayment of past amounts due. In contrast, the PCAs who are paid by commissions have the reverse incentive. There is no commission given to PCAs when they work with a taxpayer to increase his or her withholding. If a taxpayer increases withholdings, he or she may not be able to afford to pay a delinquency from a prior tax year. Moreover, since PCAs are paid as a percentage of the taxes actually collected, there is an incentive to close accounts through full-pays or high-dollar monthly installments. There is less incentive to take into consideration the taxpayer's specific circumstances. Unreasonable installment agreements result in defaults, and can harm taxpayers' ability to become compliant. It is inevitable that the effect of these incentives will be adverse to taxpayer compliance in some cases.

Some proponents of the PDC initiative have touted the outsourcing of collection by the states and the Department of Education in support of the IRS's use of PCAs. We find these arguments unpersuasive. The Department of Education and most State Departments of Revenue do not have large collection functions. The IRS, on the other hand, has allocated over 14,000 FTEs to its collection initiatives and, as noted, has an annual collection budget of over \$2 billion. Moreover, IRS employees are subject to many taxpayer protections, above and beyond the requirements of the FDPCA, that do not apply to either state PCA arrangements or the Department of Education.

These taxpayer protections exist for several reasons. First, taxes are the lifeblood of the Federal Government—without taxes, the government is unable to conduct the business of the people. Second, taxpayers pay their taxes willingly (if not joyfully) because they have a social contract with their government—and the government's end of that contract is that it will treat its taxpayers courteously, fairly, efficiently,

<sup>68</sup> IRM 5.14.5.2 (Jul. 12, 2005). The IRS may approve streamlined installment agreements where the aggregate unpaid balance of tax liabilities is \$25,000 or less and can be fully paid within 60 months or prior to the Collection Statute Expiration Date, whichever comes first. These agreements do not require detailed financial statements or approval by IRS managers and may be granted even though the taxpayer may be able to fully pay the tax balance sooner.

<sup>69</sup> Streamlined IAs accounted for 96.7 percent of all IAs approved in FY 2006 and 96.2 percent of the open IA inventory at the close of the fiscal year. Internal Revenue Service, Collection Activity Report, Taxpayer Delinquent Account Cumulative Report, NO-5000-6 (October 2, 2006).

and helpfully. For the reasons discussed in the foregoing testimony, the PDC initiative breaches that social contract on all counts.

#### IX .Conclusion

I believe the PDC program risks too much for too little. In 1998, Congress enacted significant taxpayer rights protections to guard against overzealous IRS collection tactics. Now, less than ten years later, the IRS is outsourcing tax collection to private companies with a profit motive to extract every dollar possible from taxpayers. Calling scripts that emphasize the use of psychological techniques (e.g., “The next person to speak loses”; a well timed pause will pressure a taxpayer to “tell you everything you need to know to ‘close the sale’”) make this point clear. In addition, private collectors are constitutionally barred from discussing collection alternatives with taxpayers who cannot afford to make full payment, and this restriction further highlights a significant limitation of the program.

But even leaving aside the taxpayer rights concerns the program raises, the business case for the program does not justify its existence. Originally, the program was billed as a way for the IRS to collect essentially “free money.” The IRS would outsource tax debts it otherwise would not get around to collecting due to resource constraints, and even after commissions of up to 25 percent were paid to the PCAs, the government would receive at least 75 percent of whatever was collected.

The reality has turned out to be very different. The IRS has to spend significant sums of money to administer the program, and if these sums were instead spent to fund additional IRS enforcement personnel, the IRS may well be collecting significantly more tax debts than the PCAs will collect—even without accounting for PCA commissions. Moreover, as the inventory of PDC-eligible “easy cases” dwindles, the IRS will be outsourcing more complex cases, which will result in a lower rate of collection, higher administrative costs for the IRS, and a greater risk of taxpayer rights violations.

For the reasons I have described, I urge the Congress to terminate the PDC program now.

Pioneer Credit Recovery, Inc.      TIRNO-06-K-00181  
 Contract No. GS23F0217K



## THE INITIAL DEMAND

- \*Get the Taxpayer on the phone
- \*Verify Name and SSN, Note: if it is regarding a jointly filed and you have identified the secondary filer, you must verify both Primary and Secondary SSN information

Hello, My name is \_\_\_\_\_ and I work for Pioneer Credit Recovery, Inc. My employee number is \_\_\_\_\_, I am calling regarding an outstanding IRS tax liability for \_\_\_\_\_ (account details including applicable tax years). I would like to help resolve the outstanding balance. Your balance of \$\_\_\_\_\_ is due in full today. How can I help you to resolve this?

\*Psychological pause—let the Taxpayer speak first

IF YES (which should be the case 99% of the time)

GREAT...Before we continue, federal law requires me to inform you that this is an attempt to collect a debt, any information obtained will be used for that purpose.

Now, \_\_\_\_\_ (Taxpayer's name) let me go ahead and update your file.

\*Take the Taxpayer through the financial statement from top to bottom

### ONCE ALL INFORMATION IS OBTAINED:

O.K. \_\_\_\_\_ (Taxpayer's name) based on the information you provided me, it appears you may be able to borrow the money to pay this past due obligation.

\*Give the Taxpayer some ideas on how to borrow. Use the information from the financial statement.

#### Money Sources:

401K	Employer Loan	Credit Union
Credit Card	Bank or finance Co.	2 <sup>nd</sup> Mortgage
Co-Signer	Family	Friends
Stocks	Bonds	CD's

### IF THE TAXPAYER ATTEMPTS TO BORROW AND IS UNABLE:

Ask: "How much can you get together by \_\_\_\_\_ (end of the month) \_\_\_\_\_" and get a 2<sup>nd</sup> talk-off

## Appendix B: Training Materials for Linebarger Goggan

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Appendix E

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Linebarger Goggan PCA Training Plan TIRNO-06-K-00179

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## Telephone Techniques

Two ACA-produced training tools are used to teach collectors appropriate telephone techniques. The first tool, Professional Telephone Collection Techniques, is an interactive software package that each new collector completes. The second is Advanced Telephone Collecting, a video package, which is supplemented by worksheets completed by the collectors.

### I. COLLECTOR AND CONSUMER

- \* The Successful Collector

- Characteristics

- Sounds of Success

- \* Consumer Characteristics

- Where the Money Goes

- Causes of Debt

- \* Tough Collection Situations

- \* The Maslow Model

- Self-fulfillment

- Esteem

- Social

- Security

- Physical

- \* Consumer Appeals

- Honesty

- Pride

- Anxiety

Linebarger Goggin PCA Training Plan TIRNO-06-K-00179**II. PREPARING FOR THE CALL**

- Check the taxpayer's payment record
- Review past responses to collection attempts
- Plan your strategy
- Determine your bottom line
- Prepare your questions

**III. EIGHT STEPS OF COLLECTION (BASIC)**

- Identify the debtor [inbound and outbound]:

Be careful to discuss the debt only with the obligated parties unless you have prior consent from the taxpayer.

Always refer to the taxpayer using the proper salutation.

- Identify yourself:

Refer to yourself as Mr. or Mrs.

Make sure the taxpayer knows your name and who you represent.

- Ask for payment in full:

Identify the debt, describing it in detail.

Specify the exact amount owed.

Assume that the taxpayer will pay that amount.

- Use the psychological pause [pregnant pause]:

Once you ask for payment in full, pause for the taxpayer's response.  
↳ Silence will work in your favor.

- Identifying stalls and objections (problems):

Is it realistic?

Bad time to talk

Not my debt

Won't pay penalties and interest

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Linebarger Goggan PCA Training Plan TIRNO-06-K-00179

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Already sent payment

If the taxpayer disputes the debt, define the reason for the dispute.

\* Find a solution:

Negotiation techniques

Know your business.

Establish issues of agreement.

Verify the facts.

Discover the areas of disagreement.

\* Close the call:

Payment agreed

Make sure the taxpayer has the exact terms and the payment address and understands that you will expect the agreement to be handled as promised.

No payment

Recap the call to ensure accuracy of expectations.

\* Update taxpayer file

#### IV. SAMPLE PHONE SCRIPT

Is (taxpayer name) there?

This is (agent's name) from Linebarger Goggan Blair & Sampson calling in regard to your outstanding tax obligation with the Internal Revenue Service. This communication is from a debt collector and is an attempt to collect a debt. Any information obtained will be used for that purpose.

Your account has achieved delinquency status and has been placed in my office for immediate action. Your balance of \$\_\_\_\_\_ is due. What are your intentions regarding payment on your account?

\* Psychological pause:

The next person to speak loses.

Uuebarger Goggan PCA Training Plan TIRNO-06-K-00179

## \* Financial (does not need to be completed if debtor is paying in full):

Let me see if I can help you. First I need to update my file:

## Income:

What is the name of your present employer?

What is your direct work phone number?

Does your spouse work?

What is your household net (take home) monthly income?

When is the date of your next payday?

How do you pay your bills i.e. check, money order?

## Expenses:

How much is your monthly rent/mortgage?

How much is your monthly car payment?

How much do you pay for your utilities monthly?

How much are your total monthly credit card payments or other financial obligations?

## Net:

I show you have \$ \_\_\_\_\_ income and your expenses total \$ \_\_\_\_\_. At this time your disposable income is \$ \_\_\_\_\_.

## \* Negotiations:

Taxpayer has a checking account/credit card

Your payment of \$ \_\_\_\_\_ needs to be paid. We need to set up an ACH (check by phone) / credit card (Visa/Mastercard) payment to take care of your outstanding balance.

Please get your checkbook/credit card so we may complete the payment. What date in the next five business days do you want to use for this payment?

Linecharger Goggin PCA Training Plan TIRNO-06-K-00179

Complete the ACH/credit card transaction. Verify payment date and amount with debtor so they are clear.

Taxpayer has no checking account/credit card

Due to the delinquent nature of your account, I need you to Quick Collect the payment of \$\_\_\_\_\_ to me today. Please get a pen and paper so I may give you the proper information for your Western Union payment. You will be sending your commitment of \$\_\_\_\_\_ on (today's date).

\* Customer refusal:

How do you propose to bring this tax obligation current? I can hold your account in my office for three days. If an arrangement for payment is not established by \_\_\_\_\_ (today + three days at noon), I will mark your account as refusal to pay and refer your account for further activity. If you wish to discuss payment options, please call our 800 number (800 XXX-XXXX). Thank you and goodbye.

\*If customer changes his/her mind, negotiate payment plan within the next two weeks.

\* Closing:

Your next payment will be due (date due). Any payments received after your due date are subject to penalty and fees. Please include your account number on all payments and allow ten days' mailing time.

Should the occasion arise where you are unable to make payment, you must contact this office and notify your account officer.

Thank you for your payment arrangement (or payment).

If this is the first contact with the taxpayer, provide information on the Taxpayer Advocate Service.

**Collector's Resource Guide to Success**

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**Eight Steps to a Collection Call**

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8. UPDATE YOUR RECORDS
7. CLOSE THE SALE
6. FIND THE SOLUTION
5. DETERMINE THE PROBLEM
4. PSYCHOLOGICAL PAUSE AND LISTEN
3. ASK FOR PAYMENT IN FULL
2. IDENTIFY YOURSELF BY NAME AND COLLECTOR NUMBER, THE IRS, THE AMOUNT OF THE BILL, AND GIVE THE MINI-MIRANDA
1. IDENTIFY THE TAXPAYER, THEIR ADDRESS, SOCIAL SECURITY NUMBER AND PHONE NUMBER

If initial call, make sure to inform the taxpayer of TAS and perform a Full Compliance Check!

## Collector's Resource Guide to Success

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**Step 1: Identify The Taxpayer, Their Address, Social Security Number And Phone Number (if inbound)**

You must make sure that you are talking to the appropriate person responsible for taking care of the account. Make sure to inquire if they are a Junior or a Senior, or any other identifying information. Once you are talking to the responsible party, verify the address we show as being current and any other location information. Verify the taxpayer's Social Security Number. If they are the secondary taxpayer, verify both their Social Security Number, as well as the primary's Social Security Number. If they do not have that information, they must call back when they do. If the taxpayer is not home make sure that you leave an appropriate message with another person at home or on the answering machine.

**Step 2: Identify Yourself, the who you represent and the Amount of the Bill**

Always inform the taxpayer who you are by your name as well as collector number, where you are calling from, who you are calling for and the amount of the bill. It may be necessary to identify yourself to the person who answers the phone in order to get the taxpayer on the line. Do not tell a third party that you are calling from The CBE Group or that you are collecting on a debt. Your voice should be friendly when asking for the taxpayer by their first name.

**Step 3: Ask for Payment in Full**

Make sure this request is courteous but firm. If you think about it, to ask for anything other than payment in full is insulting. You are making an assumption that the taxpayer can't pay. Always word your demand in a way to solicit a positive response. Sometimes it's helpful to give the taxpayer two alternatives, both of which will produce a positive response. An example might be "We called to see if you have received our statement and to answer any questions you may have before you pay this in full. " If no questions then, "Great, then how would you like to take care of this today? Give the request a definite sense of urgency. Always get and give specific dates and remain in control.

**Step 4: Psychological Pause and Listen**

This pause is the most powerful part of your call. This silence shifts the burden of the conversation to the taxpayer, and they, in turn, will tell you everything you need to know to "close the sale." When you use the psychological pause, make sure you have left a question or statement to be answered.

Listening to their response is just as important. Listening is one of the most prominent assets an IRS Collector can have. Experienced collectors find that the more skilled they become, the less they talk and the more they listen.

## Appendix D: Proposed Expansion of Cases to Be Sent to PCAs

Inventory available without additional programming:			
Type of Case	Description of Case	Volume	TAS Concerns
Shelved Taxpayer Delinquent Investigation (TDI).	Delinquent returns but policy decision made to shelf the TDI.	60,822	Will create the need for PCA employees to secure returns.  PCA employees cannot determine which taxpayers are required to file tax returns, resulting in increased case referrals back to IRS to work.
Deferred (Status 23).	Balance due is below tolerance level..	595,065	Low dollar inventory may have higher percentage of low income taxpayers who do not have representation.  Low dollar accounts may cause PCAs to be more aggressive in order to make up for low dollars per case by volume closed.
Status 22	Balance due case assigned to ACS.	34,458	IRS has not completed ACS processing on these cases. Cases never intended to be sent to the PCAs are now being considered to meet the inventory and revenue projections of the PCA program.
U.S. Territories/ Possessions.	Tax accounts for taxpayers residing in U.S. Territories/ Possessions. These accounts were originally excluded from primary inventory assignment criteria..	15,000	Complex issues, with increased likelihood of cases referred back to IRS for resolution.
Collection Statute Expiration Date (CSED) expansion > 2 years.	Current criteria is CSED>3 years. The change to 2 years will result in older cases being sent to PCAs..	150,000	Complex issues, with increased likelihood of cases referred back to IRS for resolution.
Taxpayer Delinquent Account (TDA)/Taxpayer Delinquent Investigation (TDI) Combination.	Balance due account with an associated TDI indicating there are also years where there is no record of a return..	154,612	Complex issues and the need for the PCA employee to secure delinquent returns.

Inventory available without additional programming:			
Type of Case	Description of Case	Volume	TAS Concerns
Master File Tax Code (MFT) 29.	10% IRS early withdrawal penalty on an Individual Retirement Plan..	Total number of MFT 29 and MFT 31 cases is 42,368..	Both MFT 29 and MFT 31 involve complex issues, with increased likelihood of cases referred back to IRS for resolution.  Issues likely to involve hardship, financial difficulty, spousal abuse.
Master File Tax Code (MFT) 31.	This MFT is used when IRS splits a 1040 joint tax liability and substitutes a single liability for each person and is used for such cases as innocent spouse, bankruptcy, offer-in-compromise, and Tax Court cases..		
Master File Tax Code (MFT) 55.	Miscellaneous civil penalty cases (Trust Fund Recovery penalty is most common).	36,062	Complex issues. On trust fund recovery penalty, underlying liability is the result of unpaid corporate trust fund taxes. These cases usually involve disputed facts and are hotly contested.

#### Appendix E: Analysis of PCA Cases Received in TAS to Date

##### **Summary of PDC Activity in TAS through 5/21/2007:**

Number of PDC calls received on the TAS intake telephone line (1-877-ASK-TAS1) from 9/11/2006—5/14/2007—220 calls.

Number of PDC cases received in TAS from 9/11/2006—05/21/2007—318 cases (76 are open and 242 closed).

##### **Information on TAS PDC cases:**

157 cases were a result of the PCA preparing a form (Form 911) for a TAS referral and forwarding the form to the IRS contact (the COTR) to input the TAS referral.

113 cases were added by a TAS employee answering the 1-877-ASK-TAS1 telephone line.

18 cases were the result of the Form 911 being received directly in a local TAS office.

21 cases were referred by an employee in the Wage and Investment Operating Division.

4 cases were referred by a National Taxpayer Advocate toll-free assistior.

5 cases were a result of other sources.

##### **PCA Assignment:**

#1—Pioneer Credit Recovery, Inc—69 cases

#2—LGBS, LLP—102 cases

#3—CBE Group—147 cases

##### **TAS Cases by TAS Criteria Code:**

Criteria 1—(Economic Harm)—70 cases

Criteria 2—(Adverse Action)—10 cases

Criteria 4—(Irreparable Injury)—5 cases

Criteria 5—(Delay of More than 30 Days)—50 cases

Criteria 6—(No Response/Resolution by Date Promised)—7 cases

Criteria 7—(Systemic or Procedural Failure)—154 cases

Criteria 9—(Public Policy)—19 cases

Criteria 3 and 8—(Significant Cost/Equitable Treatment or Taxpayer Rights Issues)—3 cases combined

**Summary of Issues:**

(The issues listed below were determined upon case receipt in TAS)

Potential unable to pay cases—101 cases; Potential installment agreements—38 cases; Taxpayer disputes or requests an explanation of the balance due—75 cases; Amended return issues—18 cases; Penalty and/or interest abatement requests—18 cases; Earned Income Tax Credit issue—8 cases; Levy issue—11 cases; Offer in compromise issue—7 cases; Request for assistance in filing returns—9 cases; Innocent spouse issue—3 cases; Potential identity theft cases—7 cases; Lien issue—7 cases; Appeals issue—3 cases; Bankruptcy issue—5 cases; Refund issue—5 cases; Other—3 cases.

In 58 cases, the taxpayer indicated that he or she previously contacted IRS to resolve the tax issue.

In 20 cases, the taxpayer indicated that he or she wanted to work with the IRS, not the PCA.

In 44 cases, the taxpayer requested TAS assistance when contacted by the PCA.

In 7 cases, the taxpayer had a complaint about the PCA.

**Summary of closing actions:**

Out of the 242 TAS cases that have been closed:

In 101 cases, the case was closed after TAS had completed all possible actions and the taxpayer did not respond to the Case Advocate.

In 34 cases, TAS provided the taxpayer with an explanation of the balance due, an IRS or PCA procedure, or a copy of an IRS transcript.

In 79 cases, the case was resolved with an installment agreement, a determination that the account is currently not collectible, an adjustment, an offer in compromise, a penalty abatement, an appeals request, or full payment.

In the remaining 28 cases, the case was either recalled from the PCA or the taxpayer he or she would work directly with the PCA.

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Chairman RANGEL. Thank you. Our next witness is Colleen Kelley, President of the National Treasury Employees Union, and she is with Elizabeth Paray. You may proceed.

**STATEMENT OF COLLEEN M. KELLEY, PRESIDENT, NATIONAL TREASURY EMPLOYEES UNION, ACCOMPANIED BY ELIZABETH PARAY**

Ms. KELLEY. Thank you very much. Chairman Rangel, Ranking Member McCrery, and Members of the Committee. Thank you for allowing me to provide comments on the IRS' private collection on behalf of the National Treasury Employees Union. Joining me today is Elizabeth Paray, an NTEU member and an IRS collection representative in the IRS Appletree call center in Buffalo, New York. Liz has been with the IRS since 1999, has been a certified instructor since 2002 and was named her site's 2006 instructor of the year. NTEU strongly opposes the administration's private tax collection program. It is a waste of taxpayer dollars and invites overly aggressive techniques, jeopardizes the financial privacy of American taxpayers and may ultimately serve to undermine IRS enforcement and compliance efforts. With regard to cost, former IRS Commissioner Mark Everson has repeatedly acknowledged that using private collection companies to collect Federal taxes is more expensive than having IRS do the work itself.

IRS estimates the return on investment for pursuing known tax debts through phone calls by IRS employees at 13 to 1 while the return on investment for private collection companies is expected to be less than 4 to 1. A 2002 report by former IRS commissioner Charles Rossotti found that assigning more IRS employees to col-

lection work could bring in roughly \$30 for every \$1 spent. Under current contracts, private collection firms are eligible to retain 21 to 24 percent of what they collect depending on the size of the case. These rates were never put up for competition, denying bidders an opportunity to make offers on terms that could have resulted in the Treasury getting a greater share of the collected revenue.

In addition to being fiscally unsound, allowing private collection agencies to collect tax debt on a commission basis flies in the face of the IRS Restructuring and Reform Act 1998 which specifically prevents employees or supervisors at the IRS from being evaluated on dollars of collections that they bring in. The idea of allowing private collection companies to collect taxes on a commission basis has been opposed by members of both parties, including President Reagan's Treasury Department, which said about such a proposal, and I quote, "the Department strongly opposes contracting out the collection of taxes. The public must be assured at all times that the person collecting taxes derives no personal benefits from that activity and that the integrity of the tax system will not be compromised."

IRS employees are trained to, quote, "assist taxpayers in resolving their balance due accounts." The IRS employees' interest is in helping the taxpayer to become compliant and they have access to the information as well as the enforcement tools both carrots and sticks to do that. In contrast, private collectors' interests is to collect from the taxpayer the balance due.

They have no interest in whether the taxpayer owes other taxes or may not have filed required returns, nor do they have access to any other taxpayer records, so they are unable to answer any questions provide any advice or use any enforcement tools, such as extensions offers, in compromise or liens or levies. Their only goal is to collect the money, and their only tool is a telephone.

As you know, this is not the first time that the IRS has tried to outsource the collection of Federal taxes. Obviously Chairman Lewis refers back to 1874. But even more recently, two pilot projects were authorized by Congress to test private collection of tax debt for 1996 and 1997. The 1996 pilot was so unsuccessful that it was canceled after 12 months, despite the fact that it was authorized and scheduled to operate for 2 years. A subsequent internal review by the IRS found that contractors participating in the pilot programs regularly violated the Fair Debt Collection Practices Act, did not adequately protect the security of personal taxpayer information, and did not bring in revenue. In fact, the pilot resulted in a \$17 million net loss. The IRS has the authority and the expertise to improve taxpayer compliance. But staffing has been slashed in recent years, resulting in an overall 36 percent decline in combined collection and examination enforcement staff between 1996 and 2003.

These staffing cuts have come at a time when the IRS workload has dramatically increased. While not proposing or fighting for adequate resources, the IRS has at the same time cited a lack of manpower as the justification for outsourcing cases to private collection companies. It makes no sense to allow private collection companies to keep a quarter of what they collect on the easiest cases, when IRS employees could be doing it at less cost. Clearly a better option

would be to provide the IRS with the resources and the staffing it needs. NTEU supports a 2 percent annual increase in staffing, roughly 1,800 position as year over a 5-year period to gradually rebuild the depleted IRS workforce.

Thank you for your leadership on this issue, Mr. Chairman. I would also like to thank Congressman Van Hollen for sponsoring bipartisan legislation to end the use of private collection agencies by the IRS. Ending the use of these PCAs is supported by every national consumer organization, the NAACP, as we heard the National Taxpayer Advocate and many others. Thank you, again, for allowing me to provide these comments, and I would be happy to answer any questions.

[The prepared statement of Ms. Kelley follows:]

**Prepared Statement of Colleen M. Kelley, President, National Treasury Employees Union, accompanied by Elizabeth Paray**

Chairman Rangel, Ranking Member McCrery, and distinguished members of the Committee, I would like to thank you for allowing me to provide comments on IRS' private tax collection program. As President of the National Treasury Employees Union (NTEU), I have the honor of representing over 150,000 Federal workers in 31 agencies, including the men and women at the IRS.

Mr. Chairman, NTEU strongly opposes the Administration's private tax collection program, as authorized by Congress in 2004 in the "American Jobs Creation Act of 2004." NTEU believes this misguided proposal is a waste of taxpayer dollars, invites overly aggressive collection techniques, jeopardizes the financial privacy of American taxpayers and may ultimately serve to undermine IRS enforcement and compliance efforts. NTEU believes the collection of taxes is an inherently governmental function that should be restricted to properly trained and proficient IRS personnel. When supported with the tools and resources they need to do their jobs, there is no one who is more reliable and who can do the work of the IRS better than IRS employees.

**COST**

There has been much debate over whether using contract employees is more costly than using trained and professional IRS employees. But in testimony before Congress, former IRS Commissioner Mark Everson repeatedly acknowledged that using private collection companies to collect Federal taxes is more expensive than having IRS do the work itself.

*"... we could do this work as cheaply or more than the private sector. As you know, we do the President's Competitive Sourcing Initiative and we look at different things all the time, different projects, and more often than not, the Government wins because it doesn't have to make a profit. So, I believe you could do this more cheaply internally."* (House Ways and Means Subcommittee on Oversight hearing on April 6, 2006)

*"The nation's chief tax collector said Wednesday that using private agencies to collect debts under a new program will cost more than hiring additional agents to do the job . . . "I admit it. I freely admit it," Everson said. (Associated Press, March 29, 2006. Quoting Everson at a House Appropriations Subcommittee).*

*"I have freely acknowledge it is more costly (to use private collection agencies) than it would be were the IRS to do it."* Senate Homeland Security and Governmental Affairs Subcommittee Hearing, September 26, 2006.

Supporters of the private tax collection program have frequently mentioned the importance of return on investment in the collections arena. I agree and a look at the numbers confirms once again that IRS employees can collect unpaid tax debts much more efficiently than private collectors. This fact was made clear by the Government Accountability Office (GAO) in testimony last year on the tax gap when it noted that as part of the IRS' effort to make the best use of its enforcement resources, it had developed rough measures of return on investment (ROI) in terms of tax revenue that it assesses from uncovering non-compliance. GAO noted that IRS estimated the ratio of estimated tax revenue gains to additional spending for pursuing known individual tax debts through phone calls is 13 to 1. (Senate Finance Subcommittee on Taxation and IRS Oversight hearing on July 26, 2006). But according to recent IRS figures, under even the most optimistic scenario, the ROI for the private collection companies is expected to reach just 4 to 1 in FY '08.

The high commission payments to the private contractors for work on the easiest to collect cases is unjustified and unnecessary. As you may know, under current contracts, private collection firms are eligible to retain 21% to 24% of what they collect, depending on the size of the case. Regrettably, the commission rates that contractors are being paid for their services were never put up for competition. Before the initial bid solicitations first went out, the IRS set commission rates at 21 to 24 percent of the revenue collected by contractors, denying bidders an opportunity to make offers on terms that would have resulted in the IRS getting a greater share of the collected revenue. Consequently, one of the companies that lost its bid for the contract filed a protest with GAO and noted in its bid protest that **"offerors were given no credit for proposing lower fees than the 'target' percentages and fee recommended by the IRS."**

#### **TAXPAYER FAIRNESS**

In addition to being fiscally unsound, the idea of allowing private collection agencies to collect tax debt on a commission basis also flies in the face of the tenets of the IRS Restructuring and Reform Act of 1998 (RRA 98). Section 1204 of the law specifically prevents employees or supervisors at the IRS from being evaluated on the amount of collections they bring in. But now, the IRS has agreed to pay private collection agencies out of their tax collection proceeds, which will clearly encourage overly aggressive tax collection techniques, the exact dynamic the 1998 law sought to avoid. Furthermore, the IRS is turning over tax collection responsibilities to an industry that has a long record of abuse. For example, in 2006, the Federal Trade Commission (FTC) received 69,204 consumer complaints about debt collection agencies—giving debt collectors the impressive title of the FTC's most complained-about industry (*FTC Annual Report 2007: Fair Debt Collection Practices Act*). Despite this track record, or maybe because of it, Congress waived all Federal Government liability for actions of these contractors when it authorized their use in the 2004 Jobs Act.

Mr. Chairman, the fear that allowing private collectors to collect tax debt on a commission basis would lead to contractor abuse was realized when the IRS recently confirmed that the agency had received more than five dozen taxpayer complaints against the three private collection companies, including an instance where a collector attempted to collect in a state in which it was not licensed to operate even though being licensed in all 50 States was a requirement of the bid request. A private collector also repeatedly called a taxpayer's previous address of record between 1 and 7 times a day for 27 days after establishing the taxpayer no longer resided at that location, a clear violation of the Fair Debt Collection Practices Act. **It is hard to understand how these kinds of violations were allowed to occur when the IRS repeatedly told Congress and the public that it would maintain extremely close oversight of this controversial program.**

#### **TRAINING & PROFESSIONALISM**

Another important area which we believe separates IRS employees from private collectors is the rigorous and comprehensive mandatory training that IRS employees receive. For example, new hires in the Automated Collection System (ACS), which the IRS itself has analogized to the use of private collectors, generally must complete an eight-week training course in a classroom setting which is complimented by three weeks of on the job training. In addition, these employees undergo mandatory annual training on topics such as confidentiality and privacy of taxpayer information, ethics awareness, taxpayer rights and computer security (*ACS Basic Modules A-1Training Course 6719-102*).

In contrast, it has been reported that some private collection personnel receive as little as two weeks of training before being allowed to handle taxpayer accounts. That National Taxpayer Advocate has previously cited concerns over the lack of training given to private collection employees in her recent annual report to congress noting that IRS plans to start assigning cases to the private collectors with the types of complexities that they were never intended to work on (pg. 51—*National Taxpayer Advocate Annual Report to Congress*). Olson went on to say that some of these cases will require the exercise of judgment and discretion and that such authority cannot be delegated to a non-governmental employee. IRS employees on the other hand have a wide range of tools at their discretion. They are able **analyze** financial statement information, research assets, enter into installment agreements, make currently not collectible determinations, and can take lien and/or levy enforcement actions.

In addition, while IRS policies, procedures and training guidelines are geared towards providing quality customer service and are open to the public, the operational plans of the private collectors emphasize the importance of collection results rather

than customer service and have been designated proprietary information, and thus have not been made public. This fact was highlighted recently by the National Taxpayer Advocate in her annual report to Congress in which she noted that while the IRS requires its telephone representatives to seek full payment, they cannot employ trickery or any device to manipulate taxpayers. And while “the training given to IRS ACS collection representatives includes an emphasis on fairness, accuracy, and taxpayer rights, we are concerned that the private collectors are using trickery, device, and belated Fair Debt Collection Practices Act warnings to take advantage of taxpayers.” (pg. 50)

Olson’s report also cited concerns about the ability of the private collection companies to meet the needs of a diverse American taxpaying public saying that “ . . . the three private collection agencies have taken next to no steps to address taxpayers with limited English proficiency.” (pg. 48). In contrast, the IRS is able to ensure that persons with limited English proficiency are able to understand and meet their tax responsibilities through its Multilingual Initiative (MLI). This service wide initiative provides written and oral assistance to Limited English Proficient (LEP) taxpayers in Spanish, Chinese, Vietnamese, Korean and Russian.

As noted previously, while the operational plans and calling scripts of the private collectors are not open to public scrutiny, the procedures and guidelines telling IRS employees how to serve taxpayers in administering the nation’s tax laws, as contained in the Internal Revenue Manual (IRM), are open to public examination and review and in fact, are available on the IRS website.

IRS employees are trained to “assist taxpayers in resolving their balance due accounts.” (*IRS Manual 5.19.1.1*) When an IRS employee calls a taxpayer, the employee has access to all of the taxpayer’s information and can answer questions and offer advice. For example, they can see whether a taxpayer has not filed a return and explain that the sooner the taxpayer makes arrangements to address filing and balance due issues the less penalty and interest they will owe. They can look at the taxpayer’s records and answer questions about why they owe a balance and what they can do about it. They can also tell the taxpayer that they are not having enough taxes withheld by their employer and need to address that or that if an ex-spouse is claiming a child as a dependent they will not also be able to receive an exemption. If a simple mistake, like a math error, has occurred, they can fix it. They can provide an extension of the time period for payment. They can make a determination that the taxpayer meets the currently not collectible requirements. They can determine whether the taxpayer may be eligible for an Offer in Compromise in which part of the balance due is foregone, or they can send the case on where a lien or levy can be imposed. The IRS employee’s interest is in helping the taxpayer become compliant and they have access to the information as well as the enforcement tools, both carrots and sticks, to do that.

In contrast, private collectors’ interest is to collect from a taxpayer the balance due amount they have been provided. They have no interest in whether the taxpayer owes other taxes or may not have filed required returns, nor do they have access to any other taxpayer records, so they are unable to answer any questions, provide any advice or use any enforcement tools, such as extensions, offers in compromise or liens or levies. Their only goal is collect the money and their only tool is the telephone. That may explain why concerns have been raised about the use of deceptive tactics when dealing with taxpayers “including use of the ‘psychological pause’ (the next person who speaks loses)” and “instructions to ‘close the sale’ which seem closer to boiler room techniques than efforts to bring taxpayers into compliance.” (*Nina Olson, House Appropriations Subcommittee on Financial Services and General Government hearing March 5, 2007*)

With the proliferation of tax scams and identity theft in recent years, the simple issue of providing the taxpayer with adequate identification has apparently been a problem for the private collection companies. IRS employees are assigned identification numbers, which they must provide to the taxpayer at the beginning of the call before they can confirm any of the taxpayer’s personal information. This is critical to ensure that scam artists trying to impersonate IRS employees are unable to obtain personal or financial information for purposes of stealing confidential information or taxpayer assets.

In order to give you an idea of the extent of taxpayer protections and variety of services that IRS employees provide to a taxpayer when discussing their delinquent account, I have attached a sample calling script at the end of my testimony.

#### ***History of Failure***

Mr. Chairman, as you know this is not the first time the IRS has tried to outsource the collection of Federal taxes. Two pilot projects were authorized by Congress to test private collection of tax debt for 1996 and 1997. The 1996 pilot was

so unsuccessful it was cancelled after 12 months, despite the fact it was authorized and scheduled to operate for two years. A subsequent review by the IRS Office of Inspector General found that contractors participating in the pilot programs regularly violated the Fair Debt Collection Practices Act, did not adequately protect the security of personal taxpayer information, and even failed to bring in a net increase in revenue. In fact, a 1997 GAO report found that private companies did not bring in anywhere near the dollars projected, and the pilot caused a \$17 million net loss.

Despite IRS assurances that it has learned from its past mistakes, two recent reports indicate otherwise. A March 2007 report by the Treasury Inspector General for Tax Administration on IRS' implementation of the private tax collection program raises a number of questions about the security of taxpayer information being stored on contractors' computer systems. The report is rife with alarming examples of data security lapses, including transmitting data over an unsecured channel, storing taxpayer data on a server used for four other contractor clients and failing to load antivirus and encryption software. The report notes that "these factors, as well as other computer and physical security issues, increase the risk that Federal tax information may be inadvertently disclosed, lost, stolen, or corrupted" (*TIGTA Audit # 2007-30-066*). These security breaches illustrate not only the risks associated with collecting and disseminating large amounts of electronic personal information, but the risk of harm or injury to consumers from identity theft crimes.

In addition, a September 2006 examination of the IRS private collection program by the Government Accountability Office (GAO) reveals that like the 1996 pilot, the program may actually lose money by the scheduled conclusion of the program's initial phase in December 2007. The report cited preliminary IRS data showing that the agency expects to collect as little as \$56 million through the end of 2007, while initial program costs are expected to surpass \$61 million. What's more, these projected costs do not even include the 21-24 percent commission fees paid to the collection agencies directly from the taxes they collect.

#### ***Negative Effect on Tax Administration***

Mr. Chairman, while the direct cost of the private tax collection program is clear, I am also worried about the potential negative effect that the private tax collection program will have on our tax administration system and taxpayer compliance. In her recent report to Congress, the National Taxpayer Advocate voiced similar concern about the unintended consequences of privatizing tax collection. Ms. Olson cited a number of "hidden costs" that private tax collection has on the tax system including reduced transparency of IRS tax collection operations, inconsistent treatment for similarly situated taxpayers, and reduced tax compliance. In addition, this concern has been voiced by members of both parties including President Reagan's Administration which said this about such a proposal:

**"The Department strongly opposes contracting out the collection of taxes because it is likely to result in considerable adverse public reaction. The public must be assured at all times that the person collecting taxes derives no personal benefits from that activity and that the integrity of the tax system will not be compromised."**

*(Treasury Dept. Statement to House Judiciary Comm. 8/8/86)*

Clearly the negative effects of contracting out tax collection to private collectors hampers the agency's ability to improve taxpayer compliance and will only serve to undermine future efforts to close the tax gap.

#### ***Opposition Widespread and Growing***

NTEU is not alone in its opposition to the IRS' private collection program. Opposition to the program has been voiced by a growing number of members of Congress, major public interest groups, tax experts, as well as the Taxpayer Advocacy Panel, a volunteer Federal advisory group—whose members are appointed by the IRS and the Treasury Department. In addition, the National Taxpayer Advocate, an independent official within the IRS recently identified the IRS private tax collection initiative as one of the most serious problems facing taxpayers and called on Congress to immediately repeal the IRS' authority to outsource tax collection work to private debt collectors (*National Taxpayer Advocate 2006 Report to Congress*). In addition, dozens of newspapers across the country, including the San Francisco Chronicle, Providence Journal, Tennessean, Indianapolis Star, and Arizona Republic have editorialized against the use of private collection agencies.

We are also supported by Representatives Chris Van Hollen, Steve Rothman and Russ Carnahan who have introduced H.R. 695, the "Taxpayer Abuse and Harassment Prevention Act of 2007." This critical bipartisan legislation would repeal the IRS's authority to enter into contracts with private sector debt collectors and ensure

that tax collection is kept in the professional and accountable hands of Federal employees. This bill currently has 126 bipartisan cosponsors.

Instead of rushing to privatize tax collection functions which jeopardizes taxpayer information, reduces potential revenue for the Federal Government and undermines efforts to close the tax gap, NTEU strongly believes the IRS should increase compliance staffing levels to ensure that the collection of taxes is restricted to properly trained and proficient IRS personnel.

**NTEU Staffing Proposal**

Mr. Chairman, history has shown that the IRS has the expertise to improve taxpayer compliance but lacks the necessary personnel and resources. The President's fiscal 2008 budget proposal trumpets the increased tax collections produced by IRS's own employees and cites the increased collections of delinquent tax debt from \$34 billion in 2002 to \$49 billion in 2006, an increase of 44 percent. Unfortunately, instead of providing additional resources to hire more enforcement staff, IRS personnel resources have been slashed in recent years resulting in an overall 36% decline in combined collection and examination function enforcement staff between 1996 and 2003. In addition, these staffing cuts have come at a time when the IRS workload has dramatically increased.

According to IRS's own annual reports and data, taxpayers filed 114.6 million returns in 1995. After a steady annual climb, eleven years later, the Service saw more than 132 million returns filed. Yet, between 1995 and 2005, total numbers of IRS employees shrunk from 114,000 to 94,000. Even more alarming is that during that period, revenue officers and revenue agents—two groups critical to IRS enforcement and compliance efforts—shrank by 32 and 23 percent respectively. Revenue officers who collect large delinquent accounts went from 8,139 to 5,462 and revenue agents who do audits fell from 16,078 to 12,355. Unfortunately, instead of reversing this trend, the IRS has continued efforts to reduce its workforce and has moved forward with downsizing in several different areas which have targeted some of the service's most productive employees.

While moving forward with drastic reductions to its enforcement and compliance staff, the IRS has at the same time cited a lack of manpower as one of the primary justifications for outsourcing cases to private collection companies. But a recent GAO report noted that as of March 1, there were only 75 total employees among the three collection companies actually working the cases. At the same time, the report notes that the IRS had allocated 65 of its own employees to monitor the program, thus the IRS is using almost as many employees to monitor the program than are actually working the cases. (GAO-06-1065 September 2006)

NTEU believes instead of expending significant resources on monitoring outside collectors that are allowed to keep up to a quarter of what they collect, the IRS should strongly consider retraining IRS employees scheduled to be laid off to do the work that is being outsourced to private collection companies. The Taxpayer Advocate has noted that there currently ongoing reductions in force of low-graded IRS employees that are capable of being trained to do the work that is being given to private collectors. One possibility might be to look at the thousands of IRS employees that are scheduled to be laid off at a number of paper processing sites over the next several years. A number of these sites already have the **infrastructure and technological capabilities to work the type of cases being turned over to the private companies. In addition, these employees have already undergone extensive background checks and have been trained on the importance of protecting the privacy of all taxpayers.** Retraining these employees would allow the IRS to collect outstanding taxes more efficiently without putting taxpayers' financial privacy at risk.

While we believe retraining IRS employees soon to lose their jobs is a sensible and fiscally sound approach to the private tax collection issue, we strongly believe the IRS must also look to address the overall staffing crisis at the service. In order to reverse this downward trend in staffing, NTEU supports a two percent annual net increase in staffing (roughly 1,885 positions per year) over a five-year period to gradually rebuild the depleted IRS workforce to pre-1998 levels. A similar idea was proposed by former IRS Commissioner Charles Rossotti in a 2002 report to the IRS Oversight Board. In the report, Rossotti quantified the workload gap in non-compliance, that is, the number of cases that should have been, but could not be acted upon because of resource limitations. Rossotti pointed out that in the area of known tax debts, assigning additional employees to collection work could bring in roughly \$30 for every \$1 spent. The Rossotti report recognized the importance of increased IRS staffing noting that due to the continued growth in IRS' workload (averaging about 1.5 to 2.0 percent per year) and the large accumulated increase in work that should be done but could not be, even aggressive productivity growth could not pos-

sibly close the compliance gap. Rossotti also recognized that for this approach to work, the budget must provide for a net increase in staffing on a sustained yearly basis and not take a "one time approach."

Although this would require a substantial financial commitment, the potential for increasing revenues, enhancing compliance and shrinking the tax gap makes it very sound budget policy. One option for funding a new staffing initiative would be to allow the IRS to hire personnel off-budget, or outside of the ordinary budget process. This is not unprecedented. In fact, Congress took exactly the same approach to funding in 1994 when Congress provided funding for the Administration's IRS Tax Compliance Initiative which sought the addition of 5,000 compliance positions for the IRS. The initiative was expected to generate in excess of \$9 billion in new revenue over five years while spending only about \$2 billion during the same period. Because of the initiative's potential to dramatically increase Federal revenue, spending for the positions was not considered in calculating appropriations that must come within annual caps.

A second option for providing funding to hire additional IRS personnel outside the ordinary budget process could be to allow IRS to retain a small portion of the revenue it collects. The statute that gives the IRS the authority to use private collection companies to collect taxes allows 25 percent of collected revenue to be returned to the companies as payment, thereby circumventing the appropriations process altogether. Clearly, there is nothing magical about revenues collected by private collection companies. If those revenues can be dedicated directly to contract payments, there is no reason some small portion of other revenues collected by the IRS could not be dedicated to funding additional staff positions to strengthen enforcement.

Mr. Chairman, in order to continue to make improvements in taxpayer services while simultaneously processing a growing number of tax returns and stabilizing collections and examinations of cases, it is imperative to reverse the severe cuts in IRS staffing levels and begin providing adequate resources to meet these challenges. With the future workload expected to continue to rise, the IRS will be under a great deal of pressure to improve customer service standards while simultaneously enforcing the nation's tax laws. NTEU believes that frontline IRS employees are the best defense against an increasing U.S. tax gap. Unfortunately, the Administration has not requested the funding necessary to close the tax gap. Congress must, therefore, act to provide IRS with the necessary staffing and a dedicated funding stream to support those additional workers.

#### ***IRS Budget***

Mr. Chairman, the final issue that I would like to discuss is the Administration's FY '08 budget request for the IRS. As you know, the IRS budget forms the foundation for what the IRS can provide to taxpayers in terms of customer service and how the agency can best fulfill its tax enforcement mission. Without an adequate budget, the IRS cannot expect continued improvement in customer service performance ratings and will be hampered in its effort to enhance taxpayer compliance. I would like to applaud the Administration for acknowledging in its FY '08 Budget in Brief (page 65) that "assisting the public to understand their tax reporting and payment obligations is the cornerstone of taxpayer compliance and is vital for maintaining public confidence in the tax system." However, I was disappointed in the Administration for failing to request a budget for FY '08 that meets the needs of the Agency to fulfill its customer service and enforcement challenges. In fact, the President's budget anticipates a "savings" equal to nearly 1,200 full-time equivalent positions, including 1,147 in enforcement and taxpayer service programs.

Although it's widely recognized that additional funding for enforcement provides a great return on the investment, the Administration seems reluctant to request an adequate budget for the IRS. In addition, as noted previously, despite citing a lack of resources as the primary rationale for contracting out a number of inherently governmental activities, such as the collection of taxes, the former Commissioner of the IRS told Congress that the IRS does not need any additional funding above the President's budget request.

NTEU believes that Congress must provide the IRS with a budget that will allow the Service to replenish the depleted workforce, particularly with respect to enforcement personnel.

Thank you again for allowing me to provide these comments on this important issue. I would be happy to answer any questions you might have.

#### ***SAMPLE IRS EMPLOYEE CALL SCRIPT***

Hello, may I speak with Jack Smith?

Hi Mr. Smith, My name is Ms. Jones, I am calling from the Internal Revenue Service, my ID # is xx-xxxxx

In order to proceed with this conversation, I need to verify some information to ensure that I am speaking with the correct taxpayer and not disclosing your information to the wrong party.

May I have your Social Security Number?

May I have your complete name as it appears on your last tax return?

What is your current mailing address?

I have reached you at your home number, can you please give me your work number?

Do you have a cell phone number?

Where are you currently employed?

And finally, where do you do your banking?

I am calling to discuss your outstanding balance (or overdue tax return). Then I proceed with the conversation—asking if they know why they owe. Are they able to full pay or borrow—if they say no, I ask why.

During the remainder of the call, I will use the ACS Quick Reference Guide to resolve all aspects of a taxpayer's account and ensure that the taxpayer receives the best possible service.

**For example, I may ask:**

What can I do to help you not owe again?

This is done to ensure that the taxpayer understands why he/she owes.

I also may state certain things to taxpayer as well, such as

- Explaining that an additional balance would default their Installment Agreement, and the consequences of default on the Agreement.
- If a taxpayer has not filed taxes for a certain year, I advise them that, under the law the IRS can file for them. This could result in the taxpayer incurring additional liability. I explain this to them to help the taxpayer avoid such a circumstance.
- In order to assist the taxpayer in filing returns, I can also send them their income information. In some instances the returns must be filed before an Installment Agreement can be set up.

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Chairman RANGEL. Thank you, Ms. Kelley. Now we will hear from Kevin Brown, who is the Acting Commissioner of the Internal Revenue Service. Thank you. Welcome to the Committee as Acting Commissioner.

**STATEMENT OF KEVIN BROWN, ACTING COMMISSIONER,  
INTERNAL REVENUE SERVICE**

Mr. BROWN. Thank you. Good morning Chairman Rangel, Ranking Member McCrery, and Members of the Committee. I appreciate the opportunity to discuss these private collection agencies for the collection of the Federal individual income taxes owed.

As you know, Mr. Chairman, the private debt collection program was authorized by the American Jobs Creation Act of 2004. The Act permitted the IRS to use collection agencies as a means for collecting delinquent taxes. It is estimated that the agencies will collect from \$1.5 billion to over \$2.2 billion over 10 years. This provides us with another tool in the effort to close the tax gap. Although there have been some growing pains in the new program, we want to do it right. We are making every effort to protect taxpayer rights. Private collection agencies and their employees are subject to extensive quality control monitoring. The employees must be in full compliance with the Federal tax laws. They also are subject to initial background checks, FBI fingerprint screening annually and a reinvestigation every 5 years. Taxpayers receive the same treatment from collection agencies that they would receive from the IRS, including access to the taxpayer advocate service.

So, far there have been no reported instances of the misuse of taxpayer information or intentional disclosure of protected information. The private collection agencies only work on cases where the taxpayer does not dispute the liability. The collection agencies cannot knock on the doors of taxpayers. They do not meet taxpayers face to face. The private companies contact taxpayers only by phone or mail. The agencies only work on cases up to \$100,000 in tax liability. The debt collection program has been examined by several government bodies. The Inspector General for tax administration reported that the IRS had effectively developed and implemented the collection program with careful attention to taxpayer rights.

The Chairman of the IRS oversight board said—and I am now quoting—overall this program seems to be working well although the board intends to continue to monitor it closely. Through this program the IRS has found a way to reach a specific segment of taxpayers who have outstanding debts. The Government Accountability Office reported that the IRS has made major progress in addressing critical success factors for the private debt collection program. The GAO also made several recommendations about how to improve the collection program and we are implementing those recommendations.

As of April 28, 2007, the private debt collection agencies have been assigned cases involving almost 38,000 taxpayers. They have collected \$19.5 million in gross revenue. Of the more than 37,000 cases placed with collection agencies we have received 25 concerns related to taxpayer treatment. That is .7 of 1 percent of all the cases assigned. Of the 25 concerns raised, only one was validated as a contract violation, two are pending the completion of an investigation, and in 22 cases there were no contract violations found. The IRS conducts customer satisfaction surveys of taxpayers contacted by private collection agencies. We have just received the survey for the month of April. Ninety-seven percent of the taxpayers who responded were satisfied with the service received from the collection agencies.

I believe that the agencies and IRS overall are taking all possible steps to treat taxpayers with fairness and respect. Mr. Chairman, the private debt collection program has made good strides. Without the collection agencies, \$19.5 million would have gone uncollected. As I noted at the start, this amount is projected to grow to the range of \$1.5 to \$2.2 billion over the next 10 years. The IRS could not collect this money otherwise. We simply do not have the manpower to make a phone call to every delinquent taxpayer in the country. Our employees are assigned to higher priority cases, requiring a deeper knowledge of the tax laws and IRS procedures. I recognize that the private debt collection program is controversial. Some Members of Congress believe the Federal tax collection is an inherently governmental function that should not be contracted out. I understand and respect those views. Nevertheless, Congress created the debt collection program and we are doing our best to carefully carry it out. Thank you, and I would be happy to take any questions you may have.

Chairman RANGEL. Thank you.

[The prepared statement of Mr. Brown follows:]

**Statement of Kevin M. Brown, Acting Commissioner, Internal Revenue Service**

Good morning Chairman Rangel, Ranking Member McCrery and Members of the Committee. I appreciate the opportunity to appear this morning to discuss the limited use of private collection agencies (PCAs) for the collection of Federal individual income tax.

As you know Mr. Chairman, the Private Debt Collection (PDC) program was authorized by the American Jobs Creation Act (AJCA) of 2004. It authorized the Internal Revenue Service (IRS) to use PCAs as an additional resource to help collect delinquent Federal taxes, addressing one aspect of the tax gap. We have proceeded based on the specific provisions of the legislation that PCAs can successfully perform some ministerial and nondiscretionary tasks in connection with the collection of taxes.

**Previous Experience**

The AJCA was not the first was not the first Act to authorize the IRS to use PCAs. In 1996 there was an initiative allowing us to create a pilot program to determine the feasibility of using PCAs. That program failed, but provided some important lessons for us in setting up the current PDC program.

First, in 1996 the assigned cases were aged and had little probability of collection (e.g., very low dollar, statute issues, etc.). This time we provided cases that have various statuses and dollar amounts. The cases also have a higher probability of collection.

Second, the pilot program did not provide systems that were specific to management of PCA activities, preventing the successful exchange of information between PCAs and the IRS. Now, we have systems in place that are more sophisticated and efficient in tracking work and addressing problems encountered with segregating the private debt-collection inventory.

Third, most of our processes and controls were manual in nature in 1996. With the current PDC program, we now have oversight and monitoring processes that are structured and efficient with increased automation for data processing and exchange.

Fourth, the pilot program allowed PCAs only to call and locate taxpayers. They had no authority to set up and monitor payment arrangements. Under our new program, maximum effort has been made to provide PCAs with the latitude required to implement best business practices in the debt-collection industry. PCAs are now authorized to request payment and set up installment agreements (with IRS approval) of up to five years in length. They also monitor case progress.

Finally, and perhaps most importantly, under the pilot program, PCAs were compensated based on a flat fee arrangement, and they were compensated even if they generated no additional collections. Under our current program, PCA payments are tied to performance.

In addition to learning from the implementation of the previous program, the tax collection climate has changed substantially since 1996. Changes in the tax law have provided greater protection for taxpayers. The landmark change was the enactment of the IRS Restructuring and Reform Act (RRA) of 1998. That act, among other things, provided for collection due process hearings for taxpayers and restrictions on productivity based evaluations of IRS employees. It also prohibited specific conduct by IRS employees and established the position of National Taxpayer Advocate.

**Taxpayer Protection**

When it authorized the program, Congress was rightly concerned that PCAs be prevented from engaging in an activity that is a violation of a taxpayer right or protection.

As such, the enabling legislative language ensures taxpayers receive the same treatment from PCAs as they would if the IRS handled their collection matters, including access to the Taxpayer Advocate Service (TAS).

Specifically, PCAs are allowed to work cases where the taxpayer does not dispute the liability. They can contact taxpayers by phone to attempt to resolve delinquent tax issue and initially were allowed to work cases from \$100 up to \$25,000. We increased the upper end of that range to \$100,000 in February. PCAs are also authorized to gather pertinent information from taxpayers and provide it to the IRS to resolve cases outside of their authority. Finally, they can use skip-tracing technology to locate taxpayers.

PCAs and their employees are subject to extensive quality control monitoring internally and by the IRS to ensure compliance with taxpayer protections and applicable policies and procedures. This oversight includes "live" monitoring of telephone

communications between collection agency employees and taxpayers, review of recorded conversations, taxpayer satisfaction surveys, audits of collection agency records, and periodic reviews of agency performance.

In addition, the IRS specifically monitors collection agency compliance with taxpayer confidentiality requirements and the restrictions on certain conduct contained in section 1203 of the IRS Restructuring and Reform Act of 1998 (RRA 1998). To date, there have been no reported instances of the misuse of taxpayer information or intentional disclosure of protected information.

In addition, private collection agencies are required to comply fully with the provisions of laws and regulations that pertain to taxpayer information, including, to the extent permissible under applicable law, the removal from the IRS contract activities of employees who violate the requirements of these provisions.

PCA employees must be in full compliance with Federal tax laws and are subject to FBI fingerprint screening annually and a reinvestigation every five years. The IRS monitors PCA compliance with all applicable Federal and State laws. Failure to comply with these laws and regulations will be considered a breach of contract.

Section 1204 of the RRA, which prohibits IRS employees from being compensated based on the number of audits they conduct or the amount of dollars they collect, does not specifically apply to the PCAs since the PCAs are not allowed to take enforcement actions. However, the intent of section 1204 was taken into account when the measurements of the PCAs were developed. For example, the IRS reviews PCAs and certifies that dollars collected are not a measure for their employee performance or their bonus structure. Also, the IRS PDC Project Director certifies 1204 compliance on a quarterly basis.

In addition, contractors are prohibited from soliciting direct receipt of funds from taxpayers. Although payments have been received at PCA sites, PCAs have fully complied with the IRS' misdirected payment requirements. Of the 114 misdirected payments sent to PCAs erroneously by taxpayers, all have been re-directed to the IRS and posted to the proper accounts.

While PCAs are held to the same guidelines of the Fair Debt Collection Practices Act (FDCPA) as IRS employees, there are many procedural differentiations and restrictions for PCAs that are in place as safeguards to minimize risks to taxpayer rights and privacy. Some of these restrictions include:

- PCAs cannot contact the taxpayer at any unusual time or place, or at a time or place an employee knows, or should know, is inconvenient to the taxpayer. (PCAs can generally contact the taxpayer after 8:00 AM and before 9:00 PM local time at the taxpayer's location, unless there is reason to know otherwise.)
- PCAs cannot contact the taxpayer at work if the taxpayer has instructed them not to do so or if there is reason to believe the employer does not allow this contact. (PCAs can call at the place of work only if permitted by a taxpayer. The IRS has not authorized any third-party contacts to date.)
- PCAs cannot contact a taxpayer directly when the IRS or the taxpayer has informed the PCA that the taxpayer has an authorized representative and the PCA is able to determine the representative's name, address, telephone number, and authority with respect to the taxpayer.
- PCAs cannot engage in conduct that is harassing, oppressive, or abusive.
- PCAs cannot visit Taxpayers.

### **Implementing the Program**

In implementing the authority granted under the AJCA to utilize private debt collectors, the IRS has been very careful both in selecting the PCAs and in ensuring that taxpayer rights were protected. We used a competitive procurement process to identify PCAs using the General Services Administration (GSA) Schedule to solicit Requests for Quotations (RFQ) for GSA debt-collection vendors.

The initial RFQ was cancelled in August 2005 as a result of a protest and re-issued in October 2005. A total of 33 firms took part in the competitive bidding process that resulted in contracts with the three PCAs selected for the limited implementation phase of the PDC program in March 2006. Prior to the contract award, the IRS researched the complaint records of the three firms with the Federal Trade Commission.

A post award protest in March 2006 delayed work until June 2006. Selected PCAs, as well as more than 350 PCA employees, passed background investigations, including tax-compliance checks. Only following the successful completion of testing and certification (including physical and information security) did the initial roll out begin.

On September 7, 2006, 11,564 cases were placed with three PCAs. This limited implementation phase was designed as a controlled environment to gather critical

information on debt collection for future releases of the program. The Taxpayer Advocate, the Governmental Accountability Office (GAO), the Treasury Inspector General for Tax Administration (TIGTA), and other vital stakeholders were included to ensure safeguards and accountability was integrated in the processes.

The following were key activities performed for project stand up:

- Usability testing of the initial contact letters with taxpayer focus groups and the capture of input from numerous stakeholders such as TAS, Counsel, Ways & Means Committee, etc.
- PCA Policy and Procedures Guide was developed and reviewed with TAS Counsel, Disclosure, and Practitioners and all PCAs who bid on the contract.
- The Quality and Reports Handbook were developed and reviewed with TAS, Counsel, and Disclosure.
- The PCA Operational Plan, PCA Training Plan, PCA Letters, and Scripts were reviewed and changes were made based on feedback from the project team, TAS, Counsel, and Disclosure.
- On-Site Management Issues Meetings were conducted with each PCA.
- Performed Business Acceptability Testing at each PCA.

During the initial months of start up, IRS representatives, the TIGTA and Disclosure were on site at the PCAs to oversee operations, answer questions about processing and ensure training was properly delivered to PCA employees.

#### **IRS Monitoring of PCA Activities**

The IRS has put in place an aggressive oversight and management process to ensure PCAs adhere to contract requirements and the protection of taxpayer rights. PDC is projected to use approximately 45 FTEs (delivered by 64 employees) in FY 2007 to provide support to the PCAs handling of taxpayers and to perform project management. Approximately 24 of these FTEs are for direct support and the remaining 21 FTEs are for project management. Since not all of the direct support employees work full-time on the project, the 24 FTEs are delivered by 43 employees. This number can vary, of course, based on workload requirements.

The employees are divided between two units—the Oversight and the Referral. The Oversight Unit (OU) has 11 full time staff—1 Manager, 1 Management Assistant, 3 Contracting Officer Technical Representatives (COTRs), 3 Management Information System (MIS) Analysts and 3 Quality Analysts.

The OU is responsible for a number of things including:

- Inventory Management: This involves the determination of the types and number of cases that should be placed with the PCAs to meet placement plans.
- Invoice Reconciliation: This includes the review of payments and administrative resolutions received and determine the amount for which the PCAs should be compensated.
- PCA Contractual Oversight: This involves the monitoring of PCAs and issues that arise including researching reported concerns to ensure adherence to the Contract. The COTR's primary role is the administration of all aspects of the contract, including invoice validation, complaint investigation, ensuring compliance with contract requirements such as background investigation review and validation, invoice computation and certification, and ensuring adherence to security requirements.
- Quality Review: This includes the monitoring of PCA phone calls and the performance of case reviews to ensure that PCAs adhere to the Policies and Procedures outlined by the IRS.
- Report Management: This involves analyzing reports and providing updates.

The Referral Unit (RU) consists of 32 employees with 2 Managers, 2 Lead Contact Representatives (CR), 2 Inventory Control Specialists, and 26 CRs.

The activities of the RU include:

- PCA Support: This includes regularly communicating with the PCA to respond or approve requests for determination on different case issues.
- Taxpayer Contact: The RU responds to request from taxpayers assigned to the PCAs. This assistance is provided to taxpayers as indicated in the letter taxpayers receive from the IRS on assignment of their case to the PCA as well as in the event the PCA may not be able to address an issue.
- Case Recall: Cases are recalled from the PCAs for a variety of reasons. This is part of the normal operating environment and provides the IRS with the ability to retrieve a case from the PCA if the case status changes where it no longer meets assignment criteria (e.g. disaster recovery).

The IRS uses processes including live-call monitoring, review of recorded telephone calls, taxpayer-satisfaction surveys, audits of PCA records and periodic review of PCA performance to assure proper safeguards are in place. Until recently, the PCAs had more than 350 employees cleared to work on this contract, with 120 to 166 front-line employees working directly on accounts.

#### **Private Debt Collection Workflow**

Once the IRS determines that a particular taxpayer module will be delivered to a PCA for collection, the IRS sends a letter advising the taxpayer that its account has been placed with the PCA. The letter identifies the PCA with whom the account has been placed as well as IRS contact information should the taxpayer have any questions. A brochure answering pertinent questions on the program is also included.

Taxpayer cases are delivered to the respective PCA electronically through a secured data exchange method. The PCA updates the files to their collection system and validates the data. PCAs perform a review of bankruptcy records or records to determine if the taxpayer is deceased.

PCAs then attempt to contact the taxpayer if they are not bankrupt or deceased. The initial contact is via letter. The PCA prepares and mails an approved initial contact letter no sooner than three business days after the IRS contact letter is mailed and no later than 10 days of receipt of inventory. The letter advises the taxpayer again that the account has been placed and provides payment and contact information for both the PCA and IRS.

The PCA will initiate phone contact with the taxpayer beginning three days after the PCA initial contact letter is mailed in an attempt to resolve outstanding debt. The taxpayer can resolve the outstanding debt either by payment of the debt in full or through an installment agreement. If the taxpayer is unwilling or unable to full pay the account or establish an installment agreement, the PCA will attempt to secure information sufficient to resolve the case and forward that information to the IRS for a case decision.

The PCA initiates electronic skip-tracing efforts to attempt to locate the taxpayer address and/or phone number. However, PCAs cannot initiate third-party contacts without prior IRS approval, and to date, that approval has not been given to any PCA. If contact with taxpayer fails to resolve the case or if electronic skip-tracing efforts fail to locate the taxpayer then the PCA may pursue additional information to resolve the case.

Collections are a difficult business whether conducted by an IRS employee or a PCA. The fact that collections are necessary at all indicates that the people are unwilling or unable to pay the debt in question. In the event a taxpayer, whose case has been assigned to a PCA, disputes the liability then the collection activity is immediately suspended by the PCA, and the case is referred to the IRS for dispute resolution.

In fact, collection activities are immediately suspended on all cases where a concern has been received by the IRS or the PCA. PCA management enters the reported concern into a log and compiles case information, which is forwarded to IRS.

#### **Handling of Concerns and Complaints**

The reported concerns process built into the PCA contracts serves as an accountability tool to identify areas where the taxpayer could be better served. Anyone may report a concern, but from our limited experience the primary source is from the PCAs directly (79%). Each PCA self-identifies cases where they believe the taxpayer may not be satisfied with the interaction they had with the PCA. This interaction is reported directly to the COTR.

All reported concerns received on PCA assigned cases are thoroughly reviewed by the PCA, the COTR and IRS review panel. Each PCA investigates every concern they identify or receive. The panel reviews documentation gathered on each case by the COTR, who also must investigate every concern. Documentation may include a case history review, discussions with the taxpayer, IRS personnel, and PCA employees, and when available, call recordings.

Depending on the severity, complaints can result in immediate contract suspension or termination. The contract includes a clause for validated penalty cases. To date, penalties totaling \$10,000 have been imposed by the IRS on the PCAs.

#### **Program Goals**

Prior to beginning implementation of the program, specific, measurable program goals and objectives were established. Specific goals include annual percent of dollars collected, case resolutions, taxpayer satisfaction, employee satisfaction, quality, and validated-penalty cases. Some of these goals cannot be measured until a full

year of performance is gained, but from what we see thus far, we are meeting or exceeding all of the goals.

There were also specific revenue projections established for the program. We projected that there would be 2.9 million cases placed for a total of \$13.9 billion through the year 2017. Original projections for gross revenue by the Office of Tax Analysis in 2004 called for the collection of \$1.5 billion to \$2.2 billion over 10 years. Based on the numbers cited below, the program is tracking toward the higher end of those projections.

#### **PCA Performance**

As of April 28, 2007, we had placed cases involving 37,689 taxpayers. Some of these taxpayers had additional tax liabilities for more than one year so there were a total of 51,414 modules assigned. The total value of the cases was \$255 million.

From these cases placed, as of April 28, 2007, 3,973 have resulted in full payment and 1,467 installment agreements have been approved. PCAs have collected \$19.49 million in gross revenue with \$15.53 million considered commissionable revenue, which resulted in \$3.38 million in payments to the PCAs. Our projections for this period of time had been to collect between \$15.05 and \$20.69 million.

Of 37,689 cases placed with PCAs through April 28, 2007, we received 25 concerns (0.07% of cases placed) related to taxpayer treatment. Of the 25 concerns raised, one was validated as a contract violation by the panel, two are pending the completion of an investigation, and in 22 cases there were no contract violations found.

Treatment concerns include 11 for PCA interaction and 14 for PCA calling practices.

Of the 11 PCA interaction concerns, six are for collector behavior (i.e., rudeness). For three of the cases, call recordings confirm professional PCA behavior. In the three other behavior cases the IRS was unable to identify a contract violation. Two of the eleven involve the taxpayer being placed on hold, and one involved the PCA not returning a call. Three are procedural issues and call recordings do not substantiate a contract violation. Two items remain open and under investigation.

Of the 14 PCA calling practices concerns, eight involve the taxpayer requesting the PCA not call them, and two involved the taxpayer being upset at receiving a call. Recordings were reviewed in five cases and PCA professional behavior was confirmed. Nine items are not representative of contract violations. Four are multiple or frequent calls to taxpayers, and one of the concerns was validated as a contract violation for which a penalty was imposed. One item remains open under investigation.

The majority of concerns are contract administration, constituting difficulties with taxpayer identity authentication or inadvertent disclosure of information. Through March 2007, 44 contract administration concerns (0.12% of cases placed) have been reported, with two validated-penalty cases (0.01% of cases placed). Of all the concerns received to date, 46% or 32 concerns were reported within 60 days of the program start up.

The PCAs have reported ten 10 disclosure concerns, all inadvertent, with only one validated contract violation penalty case by the IRS PCA Reported Concerns Review Panel. The remaining nine inadvertent disclosure cases did not rise to the level of contract violation.

#### **Costs and Benefits of the PDC Program**

In evaluating the success of this program it is important to remember the purpose for which it was created. Specifically, this program was never designed to compete with the collections that the IRS performs. Rather, it was designed to maximize the effectiveness of the PCA resources given their limited authority level. Accordingly, we select cases for PCA assignment that are not being worked by IRS employees but are still potentially collectible.

In other words, the issue is not whether the IRS or PCAs can do a better job in collecting this revenue. The issue is whether the revenue is collected by PCAs or goes uncollected. If the program ceased today, the money we are currently investing in the PDC program would *not* be reassigned to IRS employees who would then pursue these cases. It would be reassigned to employees who would go after higher priority cases, leaving the current PCA cases untouched.

Our current estimated costs for startup and ongoing maintenance of the PDC program includes all Project Office, Oversight, administration and IT costs from FY 2004 through FY 2010. To date, PDC has incurred less cost than originally budgeted in FY 2004 and, we expect it to remain cumulatively under original budget costs through FY 2010, though there likely will be some variation in total costs as the first year of operations progresses and we gain experience in complete operations.

The chart below shows the estimated budget costs between FY 2004 and FY 2010 as opposed to the actual costs

	FY 2004/ 2005	FY 2006	FY 2007	FY 2008
2004 E300 Budget Costs	\$50.07M	\$11.5M	\$11.38M	\$8.99M
2007 PDC Actual Costs and Updated Budget Costs*	\$38.87M	\$16.84M	\$14.93M	\$7.35M
Net	(\$11.2M)	\$5.34M	\$3.55M	(\$1.64M)
Cumulative Net	(\$11.2M)	(\$5.86M)	(\$2.31M)	(\$3.95M)

*\*Excludes Infrastructure Assessments*

*Updated April 30, 2007*

Based on conservative projections for revenue, the PDC program is projected to recoup all costs, including sunk costs, in April 2008. For funds allocated in FY 2007, all costs were recouped by April 2007.

Overall, the IRS Return on Investment (ROI) is about 4 to 1. ROI resulting from IRS enforcement programs ranges from \$3 to \$14 for every additional \$1 invested, depending on the type of enforcement activity. For example, labor-intensive activities such as the Collection Field Function have lower ROIs, and automated activities such as Automated Underreporter have high ROIs.

For the PDC program specifically, the potential return is between 3.2 to 1 and 3.6 to 1 for FY 2007, the first full year of implementation. This estimate is based on FY 2007 gross revenue of \$45.7 million to \$65 million, divided by the operating costs of the program, which include payments to PCAs averaging 18.5% of gross program revenues and fully loaded projected FTE costs of \$5.99 million.

In FY 2008, the IRS expects the PCA ROI will increase to between 4.0 to 1 and 4.3 to 1, once the program is in steady state. The IRS bases this estimate on FY 2008 gross revenue projections of \$86 million to \$127 million compared to operating costs of approximately \$5.84 million in IRS costs and the average 18.5% payments to the PCAs.

In a May 2004 assessment of the IRS PDC program, the GAO recommended that “the IRS Commissioner should ensure that a study is completed that compares the use of PCAs to a collection strategy that officials determine to be the most effective and efficient overall way of achieving collection goals.” In response to the GAO report, the IRS has undertaken a Cost Effectiveness Study, with input on study design from the GAO and TAS.

The study intends to analyze the cost effectiveness of the PDC program versus the use of IRS resources in working the “next best case” and compare performance between IRS and PCAs using the same types of cases currently placed with PCAs. Data will be available in June 2007 and early results will be available in September 2007, with a final report in April 2008. Data resulting from the PCA cost-effectiveness study will be used to support IRS’ response to the GAO’s recommendations, as well as the Biennial Report to Congress in late 2007.

#### GAO and TIGTA Oversight

In addition to the high level of scrutiny by the IRS, the PDC program has also been reviewed by both the GAO and TIGTA. The GAO audit focused on whether we had addressed all the critical factors for implementing a successful PDC program. The five critical factors addressed include: (1) results orientation, (2) agency resources, (3) workload, (4) taxpayer issues, and (5) evaluation.

The GAO found that the IRS made significant progress in addressing the five critical success factors and 17 related sub-factors before sending cases to PCAs for the limited implementation. The GAO identified additional steps needed on three sub-factors: setting goals and measures, determining all program costs, and evaluating the program. In response to the GAO’s findings, the IRS has developed a corrective action plan to address these sub-factors. The IRS will:

1. Establish goals and targets for all appropriate measures for FY 2008.
2. Perform a Cost Effectiveness Study; and
3. Develop reports to gather information regarding the delinquent accounts inventory, PCA resolutions based on inventory type, and IRS resource capacity.

The TIGTA has conducted two audits focusing on the development and implementation of the PDC program. The TIGTA found that the IRS effectively developed and

implemented the program and recommended actions that would enhance security and accountability.

The IRS agrees with all recommendations and will incorporate the recommendations in future contract negotiations and policy and procedural guides. These include:

- Security enhancements: During their computer and physical security review, the TIGTA identified a PCA with a shared server. The TIGTA also found other security issues that needed to be resolved but determined that these issues were not sufficiently significant to prevent the assignment of cases to the PCA. Many of the security issues identified by the TIGTA were found at the location of the PCA for whom the IRS did not extend the contract.
- In future Requests for Quotation (RFQ) we will require PCAs to maintain Federal Tax Information (FTI) on a separate dedicated server.
- We will develop procedures to ensure timely follow-up with PCAs on security issues.
- Accountability: During their review of PCA policy and procedures, the TIGTA identified areas where we could strengthen our oversight of the PCAs and our performance, including:
  - Update the procedures for handling taxpayer concerns to ensure consistent and timely processing.
  - In future RFQs, PCAs will be required to have scripts to direct employees through telephone conversations and must be submitted for review and approval.
  - As data becomes available, update/modify the revenue model used to calculate projected revenue based on the inventory placed with the PCAs.

The program has also gotten a favorable review from the IRS Oversight Board. Following its recent meeting at which the program results thus far were presented, the Board Chairman commented, "Overall, this program seems to be working well although the board intends to continue to monitor it closely. Through this program, the IRS has found a way to reach a specific segment of taxpayers who have outstanding tax debts."

#### **Evaluating the PCAs**

The initial PCA Task Orders for each of the chosen firms were issued for a 12-month period to give the IRS an opportunity to hold the PCAs accountable and to make an informed decision about moving forward with another 12-month option on a firm-by-firm basis. As we approached the time to make the decision on the contract extensions, we considered overall performance and concluded that two of the three firms met our needs and held the most accountability going forward.

In February 2007, the IRS chose to extend the contracts of two PCAs through March 2008, but declined extending the contract of Linebarger Goggan Blair Sampson, LLP (LGBS), which expired March 7, 2007. This decision demonstrates the PCA initiative is working successfully as intended, with the IRS following through on oversight responsibility and holding the PCAs accountable throughout the process.

Preparations are now underway for the June 2007 issuance of a RFQ for the next implementation phase of the PDC program. Future contractors will be selected based upon lessons learned from the limited implementation phase. The new contract award is planned for October 2007. The next implementation phase will "go-live" in March 2008.

To assist in evaluating the PCAs performance, we have developed the PCA Scorecard. This tool will be used to evaluate PCA performance by ranking PCAs on a quarterly basis

The Scorecard evaluates cases placed with the PCA for a minimum of three months, so cases placed with the PCA during the first quarter FY 2006 (October–December) could not be evaluated until April 1, 2007. The Scorecard will enable us to build incentives into the process to ensure that the companies are constantly working to improve their performance across the balanced measures. During this initial period of implementation, the scorecard process is being perfected as we establish a baseline for future use

#### **Summary**

Mr. Chairman, the PDC program has garnered controversy since its inception. A number of Members of Congress believe that Federal tax collection is an inherently governmental function that should not be contracted out. I understand and respect those opinions. Nevertheless, Congress has provided a statutory direction for the PDC program, and the IRS has carefully developed and implemented an effective

program that collects unpaid tax debts while ensuring that taxpayer rights are protected.

As the first year of this program nears completion, we believe the PDC program is operating as Congress envisioned. And, it has proved to be an effective tool in our efforts to address the tax gap, bringing in \$19.49 million in gross tax revenues to the Treasury that would have otherwise gone uncollected. Based on conservative projections for revenue, we will recoup all costs, including sunk costs, in April 2008; and we are exercising strong oversight over the program and carefully monitoring the behavior of the PCAs.

As I said earlier, collection is a tough business. Complaints are inevitable, whether we do the collections or they are done by a PCA, but in light of the over 30,000 cases that have been assigned to the PCAs, the level of complaints have been minimal, and each of those complaints have been investigated and the appropriate response undertaken.

I appreciate the opportunity to appear this morning, and I will be happy to respond to any questions.

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Chairman RANGEL. Our next witness is Thomas R. Penaluna, President and Chief Executive Officer of the CBE Group from Waterloo, Iowa.

**STATEMENT OF THOMAS PENALUNA, PRESIDENT AND CHIEF EXECUTIVE OFFICER, THE CBE GROUP, INC.**

Mr. PENALUNA. Good morning, Mr. Chairman and Members of the Committee. I thank you for providing me the opportunity to testify today. My name is Tom Penaluna. I am president and CEO of the CBE Group founded almost 75 years ago and family owned. CBE is headquartered in Waterloo, Iowa with offices in Des Moines, Iowa and Atlanta, Georgia. We currently employ over 900 people and approximately 50 of those people on the IRS private debt collection program that we are discussing here today. CBE is proud to serve a variety of organizations throughout the United States, including the Department of Education, the Financial Management Service, a bureau of the Department of Treasury, and, of course, the IRS. Serving these three agencies is an honor shared only by one other company, our colleagues, Pioneer Credit Recovery. CBE's corporate culture is based on core values of integrity respect innovation and continuous improvement. A strong work ethic is embedded in the fiber of our employees which promotes a commitment to doing things right a focus on details and a drive to deliver superior results with the highest levels of integrity which has contributed to our success in this program.

This morning I would like to describe for you our experience so far with the program, our overall views of the importance of the program and why we think it should be continued toward full implementation.

CBE continues to invest substantial resources in personnel technology and infrastructure, focused on ensuring our compliance with the strict statutory and administrative requirements in oversight that are in place to protect taxpayer rights and privacy. CBE is uses state-of-the-art systems that have been certified and accredited by the IRS. It is important to emphasize that CBE be, by statute, subject to the exact same and even greater requirements restrictions and prohibitions and legal consequences as those that are imposed upon IRS employees. In addition, we must also comply with the Fair Debt Collection Practices Act and all other laws and

regulations that govern the collection industry. Like IRS collection agents, our employees are not paid on commission basis, and must adhere closely to the call scripts that have been approved by the IRS. The program is now almost 10 months old, and it has exceeded expectations, as confirmed by independent reviews recently conducted by TIGTA, GAO and the IRS oversight board.

As with any program, there have been minor wrinkles to iron out and a few glitches along the way. However, the numbers don't lie. CBE's results are as follows: The IRS established a collection goal of 6 percent of placements recovered at the onset of the program. Today CBE has collected 8.2 percent of the dollars placed with us. The IRS established a taxpayer satisfaction goal of 67.5 percent at the onset of the program. CBE scored 97 percent taxpayer satisfaction ratings on the most recent survey taken for the month of April. The IRS established a quality goal of 90 percent. CBE's quality goal is 99.4 percent. The IRS established a goal of zero type two and type three complaints. CBE has had no type two or type three complaints, not one.

I can tell you that in the course of working over 20,000 cases through the end of last month, CBE has received only 55 alleged type one complaints for a complaint rate of less than a quarter of 1 percent, which were almost entirely self-reported and none of which have been validated by either the IRS or the taxpayer advocate service.

This is a remarkable record considering the nature of our business. CBE is extremely proud and honored to be taking part in assisting the Federal Government's efforts to reduce the national tax gap. There is no greater threat to the integrity of our tax system than the perception that tax obligation, regardless of how small the amount, can be neglected with impunity. We need to use all the tools at our disposal to collect these taxes while always respecting the privacy and rights of the American citizens.

I thank the Committee for its time and attention and would welcome your questions.

Chairman RANGEL. Thank you so much.

[The prepared statement of Mr. Penaluna follows:]

**Prepared Statement of Thomas R. Penaluna, President & Chief Executive Officer, The CBE Group, Inc., Waterloo, Iowa**

Good morning, Mr. Chairman and Members of this Committee, and thank you for providing me the opportunity to testify today. My name is Tom Penaluna, and I am the President and Chief Executive Officer of The CBE Group, Inc. Founded almost 75 years ago and family-owned, CBE is headquartered in Waterloo, Iowa. In addition to Waterloo, we have offices in Des Moines, Iowa and Atlanta, Georgia, and we currently employ over 900 people. Approximately 50 of these people work in our Waterloo offices on the IRS private debt collection program that we are discussing here today.

CBE serves a variety of organizations throughout the United States, including student loan guaranty agencies, colleges and universities, healthcare organizations, financial institutions, satellite and telecommunications companies, utilities and State and Federal Government agencies. We are proud to serve the Department of Education, the Financial Management Service—a bureau of the Department of Treasury—and, of course, the IRS. Serving all 3 of these Federal agencies is an honor shared by only one other company—Pioneer Credit Recovery, Inc.

CBE's corporate culture is based on our core values of integrity, respect, innovation, and continuous improvement. A strong work ethic also is embedded in the fiber of our employees, which promotes a strong commitment to doing things right, a focus on details, and a drive to deliver superior results. We look to the unifying force

of our core values as a source of energy and the foundation of a new paradigm to ensure a bright future for our industry, our company, those with whom we interact, and all who depend upon us. We believe that our commitment to these core values—combined with the exhaustive training that we provide to our employees—has contributed to our successful participation in the pilot phase of the IRS private debt collection program.

This morning, I would like to describe for you in some detail the process through which we entered the IRS program, our experience so far with the pilot phase of the program and, finally, our overall views on the importance of the program and why we think it should be continued towards full implementation.

In October of 2005, CBE responded to a Request for Quotes from the General Services Administration to participate in a limited implementation—or “pilot”—phase of a program to be administered by the Internal Revenue Service (“IRS”) to collect outstanding delinquent and undisputed Federal income tax obligations owed by individuals. Following an extended and very rigorous competitive bidding process, we and 2 other firms were selected from among 33 firms to participate in the pilot phase of the program.

In preparation for the start of the program’s pilot phase, CBE invested substantial resources in personnel, technology and infrastructure, with a sharp focus on ensuring that we comply in every way with the stringent statutory and administrative requirements that were designed to protect the rights and privacy of those individuals with whom the program would come into contact. The National Taxpayer Advocate, Government Accountability Office (“GAO”), Treasury Inspector General for Tax Administration (“TIGTA”) and several other government agencies were intimately involved in nearly every aspect of our extensive preparations—including the development of the training program and materials, policy and procedures guides, operational plans, form letters and other written materials, and call scripts—in order to ensure that all facets of the program were infused with appropriate safeguards and accountability.

With regard to program personnel, it is important to highlight that we are subject—by statute—to the exact same requirements, restrictions and prohibitions as those that are imposed upon IRS employees, including the provisions of the Fair Debt Collection Practices Act and the IRS Restructuring and Reform Act of 1998. The program does not confer upon our employees any IRS enforcement powers—we are only empowered to contact individuals with delinquent and undisputed tax obligations and request that they make payment to the IRS—so, of course, provisions relating to the misuse of enforcement powers such as property seizure and wage garnishment are not applicable to us. We also are subject to the same civil monetary damages as IRS employees for any unauthorized collection actions. To meet the high standard conduct outlined for this program, the only employees that we place into the IRS program are existing employees—not new hires—who already have significant experience with making outbound debt collection calls and who have never received any complaints.

Before being placed into the program, these employees must successfully complete an FBI background investigation and undergo several weeks of intensive and specialized multimedia training for this program. In addition, they must undergo a new background investigation every 5 years and must be fingerprinted by the FBI every year.

Like IRS collection personnel following enactment of the 1998 IRS reform legislation, our employees are not paid on a commission basis, which is prohibited by the terms of the program contract. In making their phone calls, these employees must adhere closely to call scripts that were approved by the IRS after having been reviewed and revised based upon comments received from the National Taxpayer Advocate. CBE has instituted and will enforce a zero tolerance policy with regard to employees that take part in this program, and the employees recognize this—as demonstrated by the fact that CBE has received no validated complaints to date in connection with this program.

The technology and physical infrastructure that we have put into place for the IRS program is standard-setting, surpassing that of even our largest corporate accounts and other government agencies, including the Department of Education and Financial Management Service. Our employees in the IRS program work in a tightly controlled and secured facility that is physically and visually isolated from the rest of our operations. Entry into this facility requires electronic access and is restricted to the employees working in the program, program managers and IRS personnel. Those who do have access to the facility are continuously monitored, are permitted to enter and leave with only limited personal belongings, and are subject to search at any time.

Working closely with IRS personnel and outside experts, we have designed and built an information technology structure for this program that features every possible security measure to protect the privacy of the information that we receive from the IRS and ensure that unauthorized persons—within or outside of CBE—cannot get access to the information. The system hardware is encrypted and relies upon a dedicated network and server that is completely segregated from the systems that we use for the rest of our operations. Of course, we do not use laptops or any other “walk away” hardware for this program.

At the same time, our technology for this program is designed to permit IRS personnel to monitor onsite or remotely live phone calls made by our employees. We also tape every phone call and retain the tapes so that they can be later reviewed by us, the IRS or the National Taxpayer Advocate for quality control purposes or in the event that an individual contacted by us lodges a complaint.

The pilot phase of the IRS program began on September 7, 2006, with the assignment of 11,654 cases to the participating firms. The program is now almost 10 months old, and we believe that the program has exceeded everyone's expectations. Independent reviews and audits recently conducted by TIGTA, GAO and the IRS Oversight Board have given the pilot phase of the program high marks overall, while noting specific areas in which the program can be further improved. In part, the success of the program so far can be attributed to the example set by other Federal Government agencies that use private collection agencies to collect delinquent debt obligations, as well as the 41 States that currently use private collection agencies to recover delinquent taxes. In particular, we have seen how the IRS program has benefited tremendously by integrating best practices and lessons learned from the Department of Education, which for well over 20 years has used private collection agencies (including CBE and Pioneer) to recover delinquent student loan obligations and has saved the Federal Government tens of billions of dollars as the guarantor on these loans.

As with any new program, there have been wrinkles to iron out and a few glitches along the way. However, the numbers don't lie. Through the end of last month, CBE has received over 20,000 cases from the IRS involving over \$125 million of delinquent taxes. We have returned to the American people over \$10 million of these delinquent taxes, while continuing to work on the remaining amount. It is important to remember that these are merely the results of the program's pilot phase, in which the caseload is only a fraction of the anticipated caseload once the program is fully implemented. From these collections, CBE was paid just over \$1 million, which means that we retained approximately 11 percent of the amount collected—not the 25 percent that is permitted by statute or asserted by critics of the program and some in the media.

Overall, the program has recovered nearly \$20 million through the end of last month, and the participating firms were paid just over \$3 million for their efforts in recovering these delinquent taxes. The legislation creating this program also permits the IRS itself to retain up to 25 percent of these recoveries—with the rest going to the general fund of the Federal Government—which means that the IRS received for its own use over \$3.5 million of the amounts recovered through the end of last month. Under the legislation, the IRS can—and we think should—use these funds to hire additional collection agents. Along with the existing IRS collections workforce, these new agents could pursue cases that are more complex and involve larger dollar amounts than the cases that are assigned to us. As these early results demonstrate, the more this program succeeds, the more everyone benefits—the participating firms, the IRS workforce and, most importantly, the American people.

It is also important to point out that we have accomplished these results using very limited information from the case files of the individuals who we contact. These files contain no tax returns or detailed tax return information whatsoever. They contain no wage or employer information. They contain no non-tax financial information. The only information that they provide is the individual's Social Security number, last known address, amount of taxes owed (as well as interest and penalties), and the tax year for which the taxes are owed. The case files do not even contain the individual's phone number, which we must locate ourselves.

Moreover, many of the traditional tools commonly used by the IRS to collect delinquent taxes are not available to us. We do not have the authority to garnish wages, seize property or enter into agreements to reduce the amount of taxes owed. We only have the authority to request the individual to pay his or her outstanding tax obligations in full or over a period of up to 5 years. These payments are made directly to the IRS—not us—so we handle no funds. In fact, we have no authority to compel an individual even to talk to us. We inform every individual who we contact that they are not required to talk to us and can request to have his or her case referred back to the IRS or to speak with the Taxpayer Advocate Service. These re-

straints under which we operate are justified by the sensitivity to privacy and taxpayer rights, but they also amplify the early success of the program.

Another key indicator of the program's success to this point is the customer service ratings that we have received from the individuals themselves who have been contacted by us to resolve their outstanding tax obligations. From a customer service standpoint, the program is monitored using taxpayer satisfaction surveys of individuals taken after they have been contacted by us. These surveys are very similar to those conducted by the IRS to evaluate its own employees who perform collection functions. The program goal for the taxpayer satisfaction survey was 67.5 percent at the onset of the pilot phase, with an ultimate goal of 90 percent. Through the end of March, the firms participating in the program have received a 94 percent taxpayer satisfaction rating.

The overall performance of the firms participating in the IRS program is measured by a quality rating, which takes into account: the results of the taxpayer satisfaction surveys; the number of reported contract complaints; the number of contract fines assessed; the number of cases referred to the Taxpayer Advocate Service; a regulatory and procedural accuracy rating; a timeliness rating; and a professionalism rating. The program goal for the quality rating is 90 percent. Through the end of March, the firms participating in the program achieved a 99 percent quality rating.

With regard to complaints that we have received during the course of the program's pilot phase, let me be clear. I am never happy to receive complaints from individuals who are contacted by our employees regarding their delinquent debts—and validated complaints are simply unacceptable. Having said this, I can tell you that in the course of working over 20,000 IRS program cases through the end of last month, CBE has received only 55 complaints—none of which have been validated by either the IRS or the Taxpayer Advocate Service and most of which have involved administrative issues not related to taxpayer rights or privacy. In fact, there have been no validated complaints received to date by either of the firms currently participating in the program. This is a remarkable record, considering the nature of our business.

The privacy of the individuals contacted by us and the protection of their information is paramount. I can report to you that there have been no instances to date of the misuse or intentional disclosure of taxpayer information.

Finally, I cannot conclude my remarks without addressing the question of program efficiency, because the critics of this program have continued to spread misinformation about the cost efficiency of using private collection agencies to recover delinquent tax obligations. As I described earlier, CBE and Pioneer are being paid less—as a percentage of collections—than authorized by statute, and it is my hope and expectation that this hearing will bring some clarity to the true costs that would be incurred by the IRS if it actually had the resources to pursue these delinquent tax obligations itself. Once these costs are better understood and then compared to our commissions, I am confident that the cost effectiveness of this program will become evident even to critics of the program.

CBE—and I'm sure Pioneer as well—is extremely proud and honored to be taking part in assisting the Federal Government's efforts to address a serious national problem. We are not bounty hunters or gangsters. We are professionals, working in partnership with the IRS to help shrink our unacceptably large tax gap.

While this program is only a small step forward in closing the tax gap, there is no greater threat to the integrity of our tax system than the perception that tax obligations—regardless of how small the amount—can be neglected with impunity. We need to use all the tools at our disposal to collect these taxes, while always respecting the privacy and rights of American citizens.

I thank the Committee for its time and attention, and I would welcome all of you to visit our offices in Waterloo to see firsthand the fine work being done by our employees who are actively engaged in this program on behalf of the American people.

At this point, I would be happy to take your questions.

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Chairman RANGEL. The last witness is Gregory Kutz, managing director, Forensic Audits and Special Investigation, U.S. Government Accountability Office. He is here with John Ryan.

**STATEMENT OF GREGORY KUTZ, MANAGING DIRECTOR, FORENSIC AUDITS AND SPECIAL INVESTIGATION, U.S. GOVERNMENT ACCOUNTABILITY OFFICE, ACCOMPANIED BY JOHN RYAN, ASSISTANT DIRECTOR**

Mr. KUTZ. Mr. Chairman and Members of the Committee, thank you for the opportunity to discuss tax debt collection. In 2006, IRS awarded three contracts to private collection agencies as part of a pilot program. My testimony today will present key facts related to taxpayer opinions about this program. Our investigation included interviewing and obtaining data from the IRS the three private collection agencies and a consulting company that administered a taxpayer survey. I will walk you through the key facts we identified using two poster boards which are on my right and for members, on your left.

I show on the first poster board from September of 2006 until February of 2007 the IRS referred over 37,000 cases to private collection agencies. According to the IRS, these cases referred were agreed to taxes that were not being worked due primarily to resource limitations. The average case was about 3 years old and \$5,000. During this period, the three collection agencies made over 250,000 outbound calls to contact taxpayers associated with these 37,000 cases. Examples of a connected call include someone answering the telephone or the collection agencies leaving a message on an answering machine. These 250,000 calls resulted in 13,000 right-party contacts. A right-party contact means that the collection agency determined that the individual that they were speaking to was one of these 37,000 cases. One reason the 250,000 calls were made to contact 13,000 taxpayers was that the IRS did not provide telephone numbers to the collection agencies.

According to IRS representatives, this was a policy decision, not a legal matter. Providing a telephone number to collection agencies we believe would significantly reduce the number of telephone calls necessary in the future. The consulting company began an automated telephone survey of right-party contacts in late November of 2006. Note the collection agency calls began in September of 2006. As a result and show on the poster board, 6,837 or 50 percent of the over 13,000 contacts were made before the survey began. The remaining 50 percent were made after the survey. A key underlying assumption for the survey was that all right-party contacts would have a chance to complete the survey. However, we could not determine how many were offered this survey because two of the three collection agencies did not keep records.

Further, two of the three collection agencies did not offer the survey to all right-party contacts. Also note that individuals whose identity could not be validated, which are referred to as incorrect contacts, were not part of the survey. The second poster board shows that for the first 3 months, 1,572 agreed to take the survey. Of these, 1,011 completed the survey. The consulting company that prepared the survey was not aware until recently that all right-party contacts had not been offered a chance to take the survey. According to IRS, beginning in April of 2007, the two remaining collection agencies began offering the survey to all right-party contacts. With respect to the survey, the overall satisfaction rate reported by the IRS of 94 to 96 percent represents the answer to 1

of 20 questions. 15 of these questions related to taxpayer satisfaction. Satisfaction ratings for these 15 questions ranged from 81 percent to 98 percent.

Also, we found that some taxpayers may have completed the survey more than once. In conclusion, I appreciate the importance of the policy matters related to the use of private collection agencies. My objective today was to provide you with facts so that you could make informed policy decisions. I also believe that something needs to be done about the type of telephone call that was played earlier in this hearing. None of us want taxpayers to somehow believe that a legitimate call made on behalf of the Federal Government is an attempt to steal their identity. Mr. Chairman, this ends my statement. I look forward to your questions.

[The prepared statement of Mr. Kutz follows:]

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**GAO** **United States Government Accountability Office**

Testimony  
Before the Committee on Ways and  
Means, House of Representatives

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For Release on Delivery  
Expected at 10:00 a.m. EDT  
Wednesday, May 23, 2007

**TAX DEBT COLLECTION**  
**Measuring Taxpayer**  
**Opinions Regarding Private**  
**Collection Agencies**

Statement of Gregory D. Kutz, Managing Director  
Forensic Audits and Special Investigations



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GAO-07-890T



### Why GAO Did This Study

Every year the Internal Revenue Service (IRS) does not collect tens of billions of dollars in delinquent taxes. In 2004, Congress authorized IRS to use private collection agencies (PCA) to help collect some of these debts. To ensure that taxpayers are treated properly and that the program achieves the desired results, IRS contracted with a consulting company to perform a survey of right party contacts—those individuals who confirmed their identity and tax debt to PCAs over the telephone. The consulting company reported overall taxpayer satisfaction ratings from 94 to 96 percent for contacts made from November 2006 through February 2007.

At the request of the Chairman, House Committee on Ways and Means, GAO attempted to obtain, for the period September 2006 through February 2007, the number of tax debt cases IRS referred to PCAs, right party contacts who were offered the taxpayer survey, and right party contacts who took the survey. GAO was also asked to report any other key observations related to the PCA program and taxpayer survey.

To perform this work, GAO collected information and interviewed officials from IRS, the consulting group that administered the survey, and the PCAs.

[www.gao.gov/cgi-bin/getrfp?GAO-07-890T](http://www.gao.gov/cgi-bin/getrfp?GAO-07-890T).

To view the full product, including the scope and methodology, click on the link above. For more information, contact Gregory D. Kutz at (202) 512-7455 or [kutzg@gao.gov](mailto:kutzg@gao.gov).

May 23, 2007

## TAX DEBT COLLECTION

### Measuring Taxpayer Opinions Regarding Private Collection Agencies

#### What GAO Found

According to the PCAs, 37,030 tax debt cases were referred to them by IRS from September 2006 through February 2007. PCAs reported making contact with, and authenticating the identity of, 13,630 right party contacts. Of these, 6,793 were eligible to take the taxpayer survey which did not start until the end of November 2006. According to the consulting company, the validity of the survey was based on the key underlying assumption that all right party contacts would be offered a chance to take the survey. However, GAO could not determine the number of right party contacts offered the survey because not all PCAs kept records on who was offered it. Further, as summarized in the following table, the three PCAs used different methods to determine which right party contacts were offered the survey.

**PCA Approaches to Survey Methodology, December 2006 through February 2007**

PCA	Number of individuals offered survey	Survey methodology	Offered survey to all right party contacts	Records kept
One	999	Primarily offered survey to all first and third contacts during specified times of day	No	Yes
Two	1,283	Offered to all right party contacts	Yes	No
Three	Unknown	Offered to all right party contacts with some exceptions	No	No

Sources: GAO and the PCAs.

Note: Right party contacts offered the survey between 11/27/06 and 11/30/06 are not included in the figures above.

The consulting company that administered the survey told GAO that between November 27, 2006, and February 28, 2007, 1,572 of the individuals offered the survey, agreed to take the survey, and 1,011 of these individuals completed the survey. A consulting company representative told GAO that the company was not aware, until several months after the survey was first offered, that the PCAs used differing methodologies for offering the survey and that not all right party contacts were offered an opportunity to complete the survey. According to IRS, beginning in April 2007, PCAs began offering the survey to all right party contacts.

Among other key observations, IRS advised GAO that they did not provide the PCAs with taxpayer telephone contact information for referred cases. As a result, in attempting to contact taxpayers by telephone, PCA representatives tried to determine the taxpayers' phone numbers through electronic searches. PCA representatives told GAO that they made a total of 252,173 outbound connected telephone calls from September 2006 through February 2007 in an attempt to make contact with the 37,030 tax debt cases IRS referred. PCAs did not offer the survey to incorrect contacts, such as individuals who provided personal information but were not authenticated as right party contacts.

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Mr. Chairman and Members of the Committee:

Thank you for the opportunity to discuss issues related to private collection agencies (PCA). Because the Internal Revenue Service (IRS) does not collect billions of dollars of delinquent taxes each year—at the end of fiscal year 2005, it estimated that \$132 billion in delinquent debt with some collection potential had gone uncollected—it supports the use of PCAs to enhance its existing collection mechanisms. In 2004, Congress authorized IRS to use PCAs to help collect tax debts in certain cases.<sup>1</sup> Based on that authority, in 2006, IRS contracted with three PCAs as a pilot program.<sup>2</sup> Before referring cases to PCAs, IRS sends notification letters to the taxpayers explaining that their cases will be handled by a PCA. Once cases are referred, PCAs must first notify taxpayers of their collection efforts by letter, and are then allowed to contact the taxpayers via telephone.<sup>3</sup> Individuals who are properly authenticated over the telephone are known as right party contacts.

According to IRS, in the first 7 months of the pilot program, PCAs helped IRS collect about \$19 million in tax debt from right party contacts—over \$3 million of which was paid to the PCAs under the terms of their contract. As we have previously reported, in addition to the collection of tax debt, providing for the proper treatment of taxpayers is a critical factor in ensuring that the PCA program achieves desired results.<sup>4</sup> In order to measure taxpayer opinion and gauge PCA performance, IRS contracted with a consulting company to perform a taxpayer survey of right party contacts. Starting on November 27, 2006, the consulting company administered an automated telephone survey to right party contacts transferred to a survey line by the PCAs. Based on this automated survey,

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<sup>1</sup>American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 881, 118 Stat. 1418 (codified at 26 U.S.C. 6306) (2004).

<sup>2</sup>Contract in this case refers to task orders issued to the three PCAs under their existing United States General Services Administration federal supply schedule contracts.

<sup>3</sup>If an authorized representative is designated on an individual's tax return, for example, a legal representative, such as a Power of Attorney, the PCA is required to contact the representative rather than the individual taxpayer. For the purposes of this report, all references to taxpayers are defined as either individual taxpayers or their representatives.

<sup>4</sup>See GAO, *Tax Debt Collection: IRS Is Addressing Critical Success Factors for Contracting Out but Will Need to Study the Best Use of Resources*, GAO-04-402 (Washington, D.C.: May 24, 2004). Also see GAO, *Tax Debt Collection: IRS Needs to Complete Steps to Help Ensure Contracting Out Achieves Desired Results and Best Use of Federal Resources*, GAO-06-1065 (Washington, D.C.: Sept. 20, 2006).

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the consulting company reported that taxpayer satisfaction with PCAs was 94 percent for November/December 2006, 94 percent for January 2007, and 96 percent for February 2007.

Given the importance of ensuring that taxpayers are treated properly, at your request, we attempted to obtain, for the period September 2006 through February 2007, the number of cases IRS referred to PCAs, right party contacts who were offered the taxpayer survey, and right party contacts who took the survey. We were also asked to report any other key observations related to the PCA program and taxpayer survey.

To perform our work, we collected data and interviewed officials from IRS, the consulting group that administered the survey, and the three PCAs. We also reviewed the statement of work for the contract between IRS and the consulting company, and contract between IRS and the three PCAs. IRS, PCAs, and the consulting company told us that the data they provided are accurate. Because we did not independently verify the data, we cannot offer an opinion on its reliability or accuracy. We did not attempt to compare the PCA program with other forms of debt collection or evaluate the performance of the program itself. In addition, based on our discussions with IRS and the entities involved in this program, we have included key observations related to the PCA program and taxpayer survey. These observations illustrate areas of concern and are not intended to offer a comprehensive analysis of the PCA program. At your request, we focused our work on the period September 2006 through February 2007. We conducted our work from April 2007 through May 2007 in accordance with the President's Council on Integrity and Efficiency's Quality Standards for Investigations.

In summary, we found the following:

- According to the PCAs, 37,030 tax debt cases were referred by IRS from September 2006 through February 2007. PCAs reported making contact with, and authenticating the identity of, 13,630 of the individuals whose cases were referred. Because the taxpayer survey was not offered until the end of November 2006, 6,793 of these right party contacts were eligible to take the survey—about 50 percent of all right party contacts made since September 2006.<sup>7</sup>

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<sup>7</sup>Right party contacts made from November 27, 2006, through November 30, 2006, are not included in this figure, although they would have been eligible to take the survey.

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- According to the consulting company, the validity of the survey was based on the key underlying assumption that all right party contacts would be offered a chance to take the survey. However, we could not obtain the number of right party contacts offered the survey because not all PCAs kept records on who was offered the survey. Additionally, the three PCAs used different methods to offer right party contacts the survey. For example, one PCA told us that the survey was offered to all right party contacts, unless the PCA representative was aware of certain limiting circumstances (e.g., the individual was contacted while driving). Another PCA told us that taxpayers were randomly selected to take the survey by using a structured method that offered the survey to every first or third contact during a specified time of day.
- The consulting company that administered the survey told us that from November 27, 2006, through February 28, 2007, 1,572 individuals agreed to take the survey, and 1,011 of these individuals completed the survey. A consulting company representative told us that the company was not aware, until several months after the survey was first offered, that the PCAs used differing methodologies for offering the survey and that, as a result, not all right party contacts were offered an opportunity to complete the survey.
- Among other related key observations, we were told that it was IRS policy to not provide the PCAs with taxpayer telephone contact information. As a result, in attempting to contact taxpayers by telephone, PCA representatives tried to determine the taxpayers' phone numbers through electronic searches. According to the PCAs, their representatives made a total of 252,173 outbound connected telephone calls from September 2006 through February 2007 in an attempt to resolve the 37,030 cases IRS referred.<sup>4</sup> Out of these 252,173 calls, PCAs confirmed 13,630 right party contacts.
- The overall satisfaction rating of 94 percent to 96 percent reported by the consulting company, and quoted by IRS, represents the answer to 1

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<sup>4</sup>According to IRS, for all PCAs, the outbound connected call figure includes any outbound phone call that connects with a person, with the exception of calls that are answered but immediately disconnected. For 2 PCAs, outbound connects include reaching an electronic answering device such as an answering machine. The third PCA's predictive dialer system does not connect identified answering machine calls to employees. Outbound connects do not include no answers, operator messages for disconnected numbers, busy signals, fax machine answers, or calls that do not connect for any other reason.

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question on the 20-question automated survey. Of the survey questions, 15 related to taxpayer satisfaction; the other questions were to gather more information about the respondents themselves. Those respondents who completed the entire survey had their results counted by the consulting company.

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## Background

As of December 2004, IRS classified approximately \$7.7 billion in delinquent tax debt as potentially available for private debt collection—\$5.5 billion in low-priority work and \$2.2 billion that was not likely to be assigned to IRS employees for collection. In the American Jobs Creation Act of 2004, Congress authorized IRS to contract with private sector debt collection companies to collect federal tax debts. Based on this authority, IRS awarded contracts in March 2006 to three PCAs for tax collection services. IRS began referring taxpayer cases to PCAs in September 2006. Because of legal restrictions, PCAs can only take certain defined steps to collect tax debts—including locating taxpayers, requesting full payment of the tax debt or offering taxpayers installment agreements if full payments cannot be made, and obtaining financial information from taxpayers. PCAs have limited authorities and are not allowed to adjust the amount of tax debts or to use enforcement powers to collect the debts, which IRS believes are inherently governmental functions to be performed only by IRS employees. Additionally, PCAs do not actually collect the debts, but instruct taxpayers to forward payments to IRS. PCAs are paid on a fee-for-service basis ranging from 21 percent to 24 percent of the debt collected based on the balance of the account at the time of referral. IRS only referred those cases in which the taxpayer had not disputed the debt (e.g., taxpayers who filed form 1040, 1040A, or 1040EZ and owe a balance) and delinquency exists for one or more tax periods.

Under the IRS policy and procedures guide, PCAs are required, within 10 calendar days of receiving delinquent account information from IRS, to send a taxpayer notification letter to an address provided by IRS. This letter states that the taxpayer's account has been placed with an IRS contractor for collection. According to IRS guidance, no sooner than 2 days after the PCA sends the notification letter, PCA employees may attempt to contact the taxpayer by telephone. However, to comply with 26 U.S.C. § 6103—which establishes a taxpayer's right to privacy of tax information—PCA employees must not disclose any tax information until they are certain the person with whom they are speaking is the taxpayer. When a PCA employee makes a call to a taxpayer and reaches an answering machine, the only information the employee may leave on a recording is his or her name (no pseudonyms), company name, telephone number, the name of the taxpayer the PCA is attempting to reach, and the

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fact that the PCA is calling about a debt (i.e., rather than specifically a tax debt).

In August 2006, IRS began working with a consulting company to develop and administer a taxpayer survey for PCA contacts. On November 27, 2006, the consulting company began administering the survey. Under guidance issued by IRS, PCAs were instructed to invite every right party contact to take the survey. If the contacts agreed to take the survey, they were transferred to the automated survey line. For the first 3 months of survey administration, the consulting company was required to issue overall satisfaction scores every month, followed by a quarterly report containing responses to all survey questions with information subdivided by each PCA.

According to IRS, early in 2007, IRS did not execute the option to renew one of the PCA contracts. As of the date of this testimony, only two of the PCAs we reviewed are now under contract with IRS.

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### PCA Program Data, Survey Data, and Key Related Findings

According to the PCAs, 37,030 tax debt cases were referred by IRS from September 2006 through February 2007. In addition, we were informed that the survey was not offered until November 27, 2006—almost 3 full months after PCAs began to contact taxpayers. PCAs reported a total number of 13,630 right party contacts from September 2006 through February 2007, with 6,793 of these contacts made after the survey was available.<sup>7</sup> Because PCAs began calling taxpayers in September 2006 before the survey was available, about 50 percent of all right party contacts identified during the period of our review were not eligible to take the survey.

According to the consulting company, the validity of the survey was based on the key underlying assumption that all right party contacts would be offered a chance to take the survey. Although IRS instructed the PCAs to offer the survey to all right party contacts, we could not obtain information on how many of the 6,793 contacts were offered the survey. One PCA reported that it offered the survey to 999 right party contacts and made 2,694 right party contacts during this period. Officials at this PCA

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<sup>7</sup>As indicated previously, right party contacts made from November 27, 2006, through November 30, 2006, are not included in this figure, although they would have been eligible to take the survey.

told us that from November 27, 2006, through February 13, 2007, taxpayers were randomly selected to take the survey using a structured method that offered the survey to every first or third contact during a specified time of day. The second PCA told us that it offered the survey to all right party contacts, but it did not keep any records to substantiate this claim. The third PCA told us that the survey was offered to all right party contacts, unless the PCA representative was aware that the contact was driving, if the contact had stated that he or she needed to get off the phone, or the contact said he or she was late for something. This PCA also did not have records regarding how many right party contacts were offered the survey, but an official noted that they were implementing procedures to track this information in the future. See table 1 for a summary of the PCA approaches to offering the survey during the period of our review.

**Table 1: PCA Approaches to Survey Methodology, November 2006 through February 2007**

PCA	Number of individuals offered survey	Survey methodology	Offered survey to all right party contacts	Records kept
Company one	999	Primarily offered survey to all first and third contacts during specified times of day	No	Yes
Company two*	1,283	Offered to all right party contacts	Yes	No
Company three	Unknown	Offered to all right party contacts with some exceptions	No	No

Sources: GAO and the PCAs.

Note: Right party contacts offered the survey between November 27, 2006 and November 30, 2006 are not included in the figures above.

\*IRS did not execute the option to renew this PCA's contract early in 2007.

Beginning in early April 2007, IRS officials reemphasized the need for PCAs to offer the survey to all right party contacts and to keep records in this regard. These instructions have been incorporated in additional guidance for the PCAs.

The consulting company that administered the survey provided us with records indicating that of those offered the survey, 1,572 right party contacts agreed to be transferred to the automated survey system from November 27, 2006, through February 28, 2007. Of these, records further indicate that 1,011 individuals completed the survey. A consulting company representative told us that the company was not aware, until several months after the survey was first offered, that the PCAs had used differing methodologies for offering the survey and that not all right party contacts were offered it. Table 2 provides summary information on the data we gathered from IRS, the PCAs, and the consulting company.

**Table 2: Summary of PCA Work and Consulting Company Survey Work, September 2006 through February 2007**

<b>Tax debt cases referred to PCAs</b>	<b>37,030</b>
Right party contacts	13,630
• During survey period <sup>a</sup>	6,793
• Offered survey	Unknown
• Agreed to be transferred to survey line	1,572
• Completed survey	1,011

Sources: IRS, the PCAs, and the consulting company.

Note: We did not independently verify the reliability of these data.

<sup>a</sup>The survey period we reviewed was from November 27, 2006, through February 28, 2007. Data do not include right party contacts made between November 27, 2006 and November 30, 2006.

We also made several related observations during the course of our work:

- PCAs were given some information about taxpayers with delinquent debt, including the taxpayers' name, Social Security numbers, and last known addresses per IRS records. According to IRS, it did not provide PCAs with telephone numbers for the taxpayers as a matter of policy. As a result, in attempting to contact taxpayers by telephone, PCA representatives tried to determine the taxpayers' phone numbers through electronic searches, for example, through the Lexis-Nexis database. PCAs told us that they made a total of 252,173 outbound connected telephone calls from September 2006 through February 2007 in an attempt to resolve the 37,030 cases referred by IRS. PCAs indicated that 89,781 calls—or about 36 percent of all connected outbound calls—resulted in messages left on answering machines, voice mail, or with third parties.
- In an attempt to make contact with the right party, PCAs may have contacted a substantial number of taxpayers who were not part of the 37,030 cases referred to PCAs by IRS—these taxpayers represent a potentially large group of incorrect contacts. Incorrect contacts were not offered the survey. Examples of individuals who were not offered the survey would include individuals who refused to provide personal information to the PCAs and individuals who provided personal information but were not authenticated as part of the 37,030 IRS referrals.
- The overall satisfaction rating reported by the consulting company, and quoted by IRS, represents the answer to 1 question on a 20-question automated survey. The question was "Everything considered, whether

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you agree or disagree with the final outcome, rate your overall satisfaction with the service you received during this call." Respondents were allowed to rate their satisfaction on a scale of one to five—with one being "very dissatisfied" and five being "very satisfied." Of the survey questions, 15 related to customer satisfaction; the other questions were to gather more information about the respondents themselves. Those respondents who completed the entire survey had their results counted by the consulting company. Satisfaction ratings for other survey questions ranged from 81 percent (ease of understanding letters received from PCAs) to 98 percent (courtesy of PCA representatives).

- Officials at IRS and the consulting company confirmed that some right party contacts were offered (and may have taken) the survey more than once because they had multiple discussions with a PCA representative. Thus, some of the 1,011 right party contacts who completed the survey may represent duplicate respondents.

Mr. Chairman, this concludes my statement. I would be pleased to answer any questions that you or other members of the Committee may have at this time.

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## Contacts and Acknowledgments

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Chairman RANGEL. Thank you so much. Mr. Brown, whose idea was this in the first place to farm out IRS collection to private organizations? How did this get started?

Mr. BROWN. Well, Congress actually enacted a law back in 2004 that allowed—

Chairman RANGEL. I know. But did they do it at the request of IRS, or did they just enact the law and tell you to do it?

Mr. BROWN. I am really not familiar with the history.

Chairman RANGEL. Are you familiar with how these firms were selected? Were there bids put out?

Mr. BROWN. Yes. There was a competitive bidding process, and three were selected at the end of that process.

Chairman RANGEL. Do you know how many people applied?

Mr. BROWN. Thirty-three.

Chairman RANGEL. Do you believe there is a special relationship between U.S. taxpayers and the IRS that is not the ordinary debtor/creditor relationship, which we all are familiar with?

Mr. BROWN. I would like to think there is a special relationship between IRS and taxpayers.

Chairman RANGEL. Do you believe, that normally the taxpayer has a certain reverence as it relates to the Internal Revenue Service rather than a tax collector?

Mr. BROWN. I would not describe my interactions with taxpayers with reverential. I am not attempting to be humorous, but it is a business.

Chairman RANGEL. You don't believe that when the IRS calls, there is a different response from the taxpayer than if just another creditor calls? When someone says an IRS agent calls, you don't think that is any different?

Mr. BROWN. I am quite frightened when an IRS agent calls me. But I would like to place in context those phone calls if I could.

Chairman RANGEL. No, no, no. We don't have that much time. Let's try to figure this out. When the IRS is collecting taxes and one of the collectors is typically good, is that person rewarded by the Internal Revenue Service for being effective? Do they get any reward for the more money they collect from the taxpayers? Is that considered?

Mr. BROWN. No. Dollars collected is not considered.

Chairman RANGEL. Do you think that it makes a difference just in everyday experience that when a person's income is dependent on the amount of money extracted and the way they handle the creditor, generally speaking?

Mr. BROWN. Well, private debt collection employees also are not compensated based on how much money they collect.

Chairman RANGEL. Then do they get a commission for the amount of money that they collect?

Mr. BROWN. No. For individual employees who make the phone calls, it is prohibited under the terms of the contract from basing their compensation, bonuses, evaluations on the amount of dollars they collect.

Chairman RANGEL. Well, in order for a firm to be successful, would it not be dependent on the amount of money they collect?

Mr. BROWN. At the firm level, that is correct.

Chairman RANGEL. So, you would call that profits. Would it be profits? The profits are dependent on the amount of money they collect?

Mr. BROWN. Yes.

Chairman RANGEL. So would it not appear as though that the more aggressive you were in collecting—strike that.

An IRS collector, do they have the taxpayer's tax files in front of them when they are collecting?

Mr. BROWN. Generally, yes.

Chairman RANGEL. Would a private collector have the tax information in front of them?

Mr. BROWN. They would have very limited information, the amount of money owed for that tax year that has been assigned to the private debt collection outfit.

Chairman RANGEL. Could the IRS person representing the government enter into settlements? Could the IRS look at the files and see if they can work out something that could be of agreement between the taxpayer and the government? Would they be authorized to do that?

Mr. BROWN. Yes. Private debt collection outfits can only -

Chairman RANGEL. No, no. I am talking about the IRS.

Mr. BROWN. I understand. The private debt collection outfits do not have authority—

Chairman RANGEL. No, no, no. I am talking about the IRS. Do they have the authority to do it?

Mr. BROWN. The IRS has authority, yes.

Chairman RANGEL. If they bring in a settlement agreement, they are not penalized because they did not collect the money?

Mr. BROWN. No.

Chairman RANGEL. The private collector, of course, on the other hand cannot reach a settlement. If they don't collect the money, they don't make the profit.

Mr. BROWN. But the private debt collection workers are also not penalized. What they do then is move to the next case.

Chairman RANGEL. But they don't make any money.

Mr. BROWN. That is correct. They wouldn't make any money on that case.

Chairman RANGEL. So, if you want to make money for the firm, you can't settle. You aggressively pursue the collection of the money owed to the government.

Mr. BROWN—full payments of the liability or an installment agreement, a full payment over time.

Chairman RANGEL. Based on your experience, if you had to negotiate a debt, would you prefer to be working with a private collector whose profits were dependent on his collection or would you want to work with an IRS collector that you are familiar with the work they do?

Mr. BROWN. Personally, I would prefer obviously not to be in debt and getting a phone call like this at all. But I would hope I could just wrap it up as quickly as possible with as little interaction with whomever was on the phone.

Chairman RANGEL. Okay. Now, your predecessor, did he have different feelings about this type of private collecting do you know? Did he support this program?

Mr. BROWN. Commissioner Everson supported this program, yes.

Chairman RANGEL. He testified before the Congress that using private collection companies to collect Federal taxes is more expensive than having the IRS to do the work itself. Do you agree?

Mr. BROWN. I agree. We have tools, our collectors—

Chairman RANGEL. Do you agree with what your predecessor said?

Mr. BROWN. I do. Our collectors—

Chairman RANGEL. —Okay. Now he also said, we could do this work as cheaply or more cheaply as the private sector. As you know, the President's Competitive Sourcing Initiative looked at different things all the time, different projects. More often than not, the government is better because it doesn't have to make a profit. So, I believe you could do this work more cheaply internally. Do you agree with that statement?

Mr. BROWN. Again,—under the law, we—

Chairman RANGEL. You have got to help me with my time. Would you say that you disagree or you agree.

Mr. BROWN. A yes or no answer doesn't fully explain—

Chairman RANGEL. That is okay. You can't answer whether you agree or disagree with that?

Mr. BROWN. We can do it more efficiently. We have tools under the law that lead's to us being more efficient.

Chairman RANGEL. If Congress provided you with the resources, could you do it more effectively?

Mr. BROWN. We would apply those resources to higher priority cases.

Chairman RANGEL. Okay. Thank you so much. He also said, I freely acknowledge it is more costly to use private collection agencies than it would be if the IRS was to do it. He said that in the Senate last year. Do you agree with that?

Mr. BROWN. Yes. We can do this more cost effectively because of the tools under the law.

Chairman RANGEL. So the Congress told you to try this method. It wasn't the commissioners who said that I could do a better job for the IRS or the government with this program. It was the Congress that told you that they wanted you to start this privatization, wasn't it?

Mr. BROWN. There was a statute enacted, yes.

Chairman RANGEL. You have been a very, very good witness. I want to thank you. I would like to yield to Mr. McCrery.

Mr. MCCRERY. Thank you, Mr. Chairman. I thought all the witnesses were very good.

Chairman RANGEL. I don't know that yet.

Mr. MCCRERY. I commend their testimony. I haven't practiced law in many years, but when I was practicing law, lawyers extract anywhere from 25 percent to 40 percent for collecting debts. What is the average, Mr. Brown, percentage take from these private debt collectors?

Mr. BROWN. 18.5 percent.

Mr. MCCRERY. 18.5. Not 25 percent?

Mr. BROWN. 18.5.

Mr. MCCRERY. 18.5 percent. I believe in response to the Chairman—one of the Chairman's questions, you were about to illustrate why this is not an apples-to-apples comparison. While yes, if we gave the IRS more resources, more money to hire more workers to collect more debts, you wouldn't put those resources toward collecting these particular debts, would you?

Mr. BROWN. No. The comparison is difficult to make.

Mr. MCCRERY. It is an apples-to-oranges comparison.

Mr. BROWN. Yes. IRS employees have the power of filing a Federal tax lien to levy on wages and bank accounts and that sort of things. The private debt collection employees do not have those powers.

Mr. MCCRERY. Thank you for explaining that, Mr. Brown. The fact is if we want to give more resources to the IRS, we can do that, or at least we can suggest that to the appropriators. That is not in our jurisdiction. But if the Appropriations Committee sees fit to give the IRS more resources that may, in fact, result in higher collections but not from the debtors that are identified for use in this particular program. Now, the TIGTA is the Treasury Inspector General For Tax Administration. What has the Treasury Inspector General found about the development and implementation of this program?

Mr. BROWN. They have said that we have effectively implemented the program. There were things we could improve but overall, we have implemented the program effectively.

Mr. MCCRERY. How about the IRS oversight board? What have been their findings?

Mr. BROWN. They think the program to date has been well run, and they want to keep an eye on it.

Mr. MCCRERY. The GAO has made some recommendations, haven't they, to the IRS for improvements? Has the IRS agreed to implement the GAO recommendations?

Mr. BROWN. We have.

Mr. MCCRERY. Mr. Kutz, is that your understanding as well, that the IRS has agreed to implement the recommendations of the GAO?

Mr. KUTZ. Yes.

Mr. MCCRERY. Are you satisfied that they are going to do that?

Mr. KUTZ. Yeah. I think the one key one is to do an apples and apples cost comparison of using private collection agencies with the other options here.

Mr. MCCRERY. That would be a good idea. Is that underway Mr. Brown?

Mr. BROWN. No. Not completely apples to apples. What we would be doing then is taking IRS employees and telling them not to use their powers, their full array of powers under the Internal Revenue Code which would then lead to less money being collected. So, what we are doing is assigning the same work to both sets of employees, both the private ones and the government employees and comparing the results there.

Mr. MCCRERY. Generally speaking, what is the potential rate of return, the IRS return on investment for collections?

Mr. BROWN. For this type of work, it would be about 13 to 1, but again I caution that the numbers are not an apples-to-apples comparison because of the tools that IRS employees have to work.

Mr. MCCRERY. Again, if you had more tools, you wouldn't utilize them for these debtors, you would go after higher targets?

Mr. BROWN. We have higher dollar cases, more recent liabilities and more complex cases that we would work on.

Mr. MCCRERY. So, essentially, Mr. Brown, it seems to me that what taxpayers are getting, what the IRS is getting is help in collecting debts that would otherwise go almost unattended to. The IRS, as I understand it, for these debtors sends four notices. Is that correct?

Mr. BROWN. Yes. I would like to place the phone calls in context. The taxpayer files a return and he admits that he owes the tax, but there is not a check that accompanies the return. We then send the taxpayers four notices over the course of about 6 months. They are increasingly severe in language. Many of them then get a phone call from the IRS. Then we send them a letter, saying that your account is now going to be assigned to a private debt collector. A few days go by, the private debt collector then sends him a letter saying your account has now been assigned to us and we will be phoning you soon. What you have heard there are phone calls where the taxpayer says they did not get the letter. We are cognizant of the fact that some people may actually not have gotten the letter for whatever reason. We are going to now send letters where we hear a conversation like that. We will send these letters by certified mail and then have private debt collectors call once again.

Mr. MCCRERY. One of the reasons the collectors are somewhat vague in identifying themselves and the subject of the call is for privacy reasons, isn't it?

Mr. BROWN. That is exactly right. Under Federal law you cannot disclose tax return information to anyone other than the taxpayer. So, the collector are quite cautious about making sure that the taxpayer is the phone and what you are hearing there is an authentication process before they want to talk about the bill.

Mr. MCCRERY. Thank you, Mr. Brown. Mr. Chairman, I have an estimate from the Joint Tax Committee of the cost to the Treasury if we were to repeal this law, which estimates that we would lose—the Treasury would lose about a little over \$1 billion over the next 10 years if we were to repeal this program. I would like to submit this estimate for the record, Mr. Chairman.

Mr. LEVIN. [Presiding.] So, ordered. I guess I am next. I will call on myself.

I don't quite understand the apples-to-apples and apples-to-oranges discussion. Let's say the tougher cases are apples and the less difficult cases are oranges. Okay? Does IRS have enough personnel to effectively enforce the law against the apples, the more difficult cases?

Mr. BROWN. No.

Mr. LEVIN. So, essentially what the minority is saying, having underfunded IRS in terms of going after the apples, that they have provided money for somebody to go after the oranges. In terms of the tax gap, what percentage of the tax gap do you think is going

to be addressed by going after what we have called the oranges through these private collection agencies?

Mr. BROWN. It would be relatively small. About \$33 billion of the tax gaps, what we call underpayments, which is a collection activity and this is going to garner—let's say it garners over \$2 billion over the course of 10 years, relatively small. I would note, though, that it is real money, \$2 billion.

Mr. LEVIN. I know. I didn't say it wasn't real money. You are a careerist, right?

Mr. BROWN. I am.

Mr. LEVIN. So, you don't have to defend either what we do or what the Republicans do, right?

Mr. BROWN. I am here just to explain how the program works.

Mr. LEVIN. Okay. No one was saying a billion isn't real money. What we are saying is, we have this tax gap, even if it isn't as large as some think, for years we have underfunded the IRS to go after what we have called the apples and significantly. So what they are saying is, apparently—I hope not all—that here we have provided private collectors moneys to go after what is a very small part of the tax gap, while they have failed to provide adequate moneys to go after those who represent the largest portion of the tax gap. Now, it is possible, is it not, for IRS employees to go after also those whom we have called the oranges? It is possible for them to do the easier work, right?

Mr. BROWN. It would be possible. We have a relative prioritization of our work, and we tend to work the harder more complex cases that are likely the more lucrative cases first.

Mr. LEVIN. Exactly. So, what has happened is, this Congress, under past leadership, has failed to fund IRS to go after the harder cases that provide—that present most of the money that has been unpaid while providing private tax companies, collectors to go after the easier cases that represent a very small portion of the tax gap.

Mr. BROWN. Well, this is to say supplement to what we do.

Mr. LEVIN. Well, you can call it a supplement. It is a replacement in the sense that if adequate moneys were provided IRS, you could go after everybody, right?

Mr. BROWN. I would—

Mr. LEVIN. You prioritize only because of inadequate funding, isn't that correct?

Mr. BROWN. Well, we prioritize because the cases tend to be better cases to work. There is a higher degree of success when you work those sorts of cases.

Mr. LEVIN. Higher degree of success and higher degree of moneys that are received. Okay. So, I think that should be made very, very, very clear.

Ms. Paray, I have just a short time. When you handle these cases, what do you do? Quickly. What is the relationship between the IRS and the taxpayer?

Ms. PARAY. Well, when we call a taxpayer, we identify ourselves as Ms. Paray, my ID number from the Internal Revenue Service, and then we go through a disclosure, getting their name, their Social Security number, their address, daytime phone number, work phone number. We tell them that we are calling regarding a Federal tax matter.

Mr. LEVIN. Do you think—is this the same procedure followed by the private collector?

Ms. PARAY. Based on the telephone call that we heard, they are not identifying themselves. If we leave a message on a taxpayer's identified answering machine, we tell them that this is Ms. Paray from the Internal Revenue Service. Please contact us back. We give the telephone number and a case reference number. We tell them by which day they need to call back.

Mr. LEVIN. Thank you. Mr. Herger?

Mr. HERGER. Thank you, Mr. Chairman. Very interesting testimony. I want to thank each of you for appearing before us today. As I think about my experience and why it is I am in public office from the private sector, one of my big concerns was that as individuals, as small businesspeople, we pay—our tax rates are too high. However, I do feel that we should be paying taxes. Certainly a big concern of mine, while on one hand we are trying to have our taxes as low as we can, those who owe taxes should be paying them. I think really the bottom line of why we are here today, excuse me, and what we hear so much in this Committee here in the last month or so has been the tax gap or that amount that people are not paying their taxes who should be paying their taxes.

Now, we hear some interesting things—Mr. Kutz, now you are with the Federal Government, aren't you? It is your job at GAO is to look and see whether we are doing it effectively, and you will give us an honest appraisal of the job we are doing, is that correct?

Mr. KUTZ. We provide you independent objective information to help you make policy decisions, yes.

Mr. HERGER. I appreciate that. So, if we look at this, and we have some \$290 billion that people are not paying their taxes, which puts a greater burden on people like I used to be who have a greater pressure to pay more taxes. So, the idea that at least to have everyone pay their fair taxes. So, we hear about the \$200 billion that is not being paid. Of this, we heard in testimony of Mr. Kutz, I think you mentioned that some \$132 billion is money that you feel perhaps could be collected of this, I believe, and you showed a very interesting chart over here. It was interesting—in just 6 months, we were able to collect \$19.5 million of this delinquent debts that were not being paid before, that we have basically—I don't know if you say we had given up on this \$200 billion.

We haven't given up on it, but certainly it is money that hadn't been being paid before. I would just like to—and you were outlining some of the initial success that we had, Mr. Kutz, on this pilot program. I would like to ask, are there ways that the programs can be improved and expanded to help collect on some of the other \$132 billion that the IRS doesn't collect? I might just also interject this. Now, I have been around the Federal Government, I have been here in this office for 20 years, and there isn't any doubt in my mind that our Federal employees on the whole do the very best job they can. But we have this huge government that is very difficult to make it work.

So, often we hear the way you make it work better is just hire more employees, just hire more Federal employees. That seems to be the answer to make it work right. Well, we know that that is not always the answer. Mr. Kutz, we are trying to go with some

of this money and allow the private sector in a—on money that we haven't been able to collect, be able to collect it. With what you have seen, do you see other ways of programs that we can improve or that can be expanded to help collect some of the rest of this \$132 billion?

Mr. KUTZ. Well, let me just say with respect to the limited look we did at this with the use of private collection agencies. One thing that we did see that could help the efficiency and effectiveness of this program has to do with giving telephone numbers to the private collection agencies. We believe that that is something that regardless of the policy debate going on here, if you use private collection agencies, they are going to collect tax debt by telephone. We believe IRS should give them a telephone number. They give them a Social Security number, they give them an address.

Mr. HERGER. It is like tying one hand behind their back. We talk about apples and oranges. We are really not giving them a chance.

Mr. KUTZ. That is why we get 250,000 phone calls for 37,000 people.

Mr. HERGER. Is there some reason we didn't give them phone the numbers?

Mr. BROWN. Yes. We didn't think the phone numbers would be good. As he explained, the accounts tend to be about 3 years old. We didn't think the numbers were good. We are going to study this recommendation. This sounds quite sensible to me.

Mr. HERGER. Okay. Well, thank you. I think we need to let this pilot program work a little further. It sounds like we are having success. We certainly need to improve on it. But I certainly would not like to see you throw this out on having everybody pay their fair share. Anyway, thank you very much.

Mr. LEVIN. Mr. McDermott has agreed Mr. Lewis will go next, the Chairman of the Subcommittee.

Mr. LEWIS. Well, thank you very much, Mr. Chairman. Thank you, Mr. McDermott. Mr. Chairman, without objection, I would like to complete the tape of where we left off.

Mr. LEVIN. Okay. Let's proceed. We will see if technology is working. It is.

[Tape is played.]

Mr. LEWIS. Mr. Chairman.

Mr. LEVIN. Yes, Mr. Lewis.

Mr. LEWIS. May I just ask Ms. Paray a question? Thank you so much for being here.

Ms. PARAY. You are welcome.

Mr. LEWIS. Would an IRS call a taxpayer's elderly parents 150 times, in some cases, up to five times a day, asking for the taxpayer when they know that the taxpayer does not live there? Would you or one of your coworkers ever do anything like that?

Ms. PARAY. No, sir. When we make the phone call, if we are told that that person is no longer there, if we have reached an incorrect telephone number, if we have reached someone where the spouse has deceased, we first apologize for reaching the wrong number if that is the case. If someone is deceased, we apologize for that, for attempting to contact them. We ask for some information regarding the deceased person.

However, when we make a phone call, we identify ourselves, that this is Ms. Paray from the Internal Revenue Service, and my ID number is—if a taxpayer chooses not to give us their Social Security number, we will tell them we understand their concern, we will offer to give them the last four of their social if we will give the first five. If they choose not to do that—and again, understandably because of Social Security theft and privacy information, we will tell them that they could call back at the 800-number we are to give them with their case reference number. When someone answers, they will know that it is the Internal Revenue Service that is calling them. We would not call them five times a day. That would not—that is not even in our guidelines to do something like that.

Mr. LEWIS. Is there anything else you would like to say or add? You heard the tape.

Ms. PARAY. As an ACS employee for the Internal Revenue Service, I am insulted that anyone would represent the government in that manner. If I received a phone call like that, I wouldn't be returning it either. There is no identification whatsoever other than a first name and a telephone number.

Mr. LEWIS. Thank you so much again for being here, coming all the way from Buffalo—

Ms. PARAY. Yes.

Mr. LEWIS. —to be here. Thank you so much.

Ms. PARAY. You are welcome.

Mr. LEWIS. Mr. Chairman if I just may ask Ms. Kelley, Ms. Kelley, thank you so much for being here, being such a good witness, and all of the witnesses for being here and for all of your help on this matter.

Do you believe there have been many, many more complaints than those reported by the private debt collectors?

Ms. KELLEY. You know, I really don't know. My understanding is these have all been self-reported, the ones that have been made available. I don't have any firsthand information otherwise about it. But I would just think that with the examples that we have heard today on the phone that there have to be—I would bet there are others that are not satisfied. I just think it puts the IRS in a terrible light. I think the credibility of the IRS is put at risk when things like that happen.

Mr. LEWIS. Ms. Olson, thank you also for being here. I know you believe there should be trust and confidence in our tax system. There must be a relationship between the taxpayer and the IRS. What do you believe?

Ms. OLSON. Well, listening to that tape, you can see that if that taxpayer finds out ultimately that it was someone hired by the IRS to call that put him through that and caused him those concerns about his identity theft, he is going to really to be concerned about how this tax system is being run. I also thought that in the course of time, that that call had took, we could have probably—if an ACS employee had been on the phone—have resolved that tax debt in that time. The PCAs do not have the tools, nor should they have the tools because they are inherently governmental to deal with taxpayers' specific circumstances and their concerns.

It is the Federal Government and the IRS employees who should be dealing with that. Although there is plenty of room for improvement, and I identify 20 most serious problems every year, pointing out that room for improvement, I believe the IRS does it better than any other tax administration system in the world.

Mr. KUTZ. Can I make one point on that? Just one clarification. There is no guarantee that that was one of the 37,000 cases in the first place. So, that is just something to consider here. That may not have been one of the taxpayers that had tax debts. There is no way to know because they didn't authenticate their identity.

Mr. CAMP. Okay. Thank you. Mr. Penaluna, is there any indication that that call is a common practice of CBE Group?

Mr. PENALUNA. Well, Congressman, I think it is important to understand that we put taxpayer privacy at the utmost in every call. The limited tools we—excuse me—the limited tools we actually have to authenticate accounts is very limited. I might also make the statement that when we leave messages on answering machines, because we are also complying with the Fair Debt Collection Practices Act, that we cannot leave the name of our company. If that third party—

Mr. CAMP. Right. But we heard comments of hundreds, 100 calls or 5 calls in a day. Are those common practices for your company?

Mr. PENALUNA. Only from the point of view that you may call somebody four or five times, not if they answered. But if they did not answer, people go to the store or are at work. So, we could call them four or five times a day until we actually reach them. Once we reach them, we will obviously do the talk off but at that point, the remaining calls would stop.

Mr. CAMP. All right. Thank you. Mr. Brown, I understood you to say the IRS sends four delinquent notices before an account is considered for referral. Then there is a letter saying your account will be referred and then another letter saying the account has been referred.

Mr. BROWN. That is correct.

Mr. CAMP. So, that is six letters then from the IRS?

Mr. BROWN. Five. Five from the IRS. One—from the PCA

Mr. CAMP. Five from the IRS, one from the private. So, six letters to the taxpayer about the delinquency.

Mr. BROWN. I should add in this situation, we just heard if the taxpayer has not received a letter, the private debt collection companies are now being instructed to send another letter by certified mail to make sure that the taxpayer do receive it. [11:30 a.m.]

Mr. CAMP. Now, if the IRS receives a call from the taxpayer, which I understand some of these letters may generate, do they—is there authentication at the same level as compared to a private collection agency?

Mr. BROWN. Yes.

Mr. CAMP. So, they have similar standards, the IRS and the private collection agency in terms of authenticating a call?

Mr. BROWN. That is correct.

Mr. CAMP. The kinds of requests for address, and as we heard testimony, partial Social Security number that we heard in the call are also done by the IRS?

Mr. BROWN. That is correct.

Mr. CAMP. But IRS employees may identify in their call a source of levy or notify the taxpayer of the potential levy or potential of issuing liens or garnishment; is that correct?

Mr. BROWN. Yes. Once we have authenticated that is actually the taxpayer, we would enter into that sort of discussion, yes.

Mr. CAMP. But private collection agencies are not authorized to identify levy sources or to notify taxpayers about garnishing wages or even the threat of those steps; is that correct?

Mr. BROWN. They have no such authority; that is correct.

Mr. CAMP. Now, there has been an IRS study that shows a 94 percent satisfaction rate for taxpayers contacted by third-party collectors. We have had some discussion about that.

Mr. BROWN. The April data indicated a 97 percent satisfaction rate.

Mr. CAMP. Ninety-seven percent. Is there a like study about the contact between IRS agents and taxpayers as well?

Mr. BROWN. The numbers are virtually identical for both our quality and what we call our customer satisfaction scores.

Mr. CAMP. So, fairly high satisfaction scores for both IRS employees as well the private collection employees?

Mr. BROWN. That is correct.

Mr. CAMP. Now, is it also correct—do I understand correctly that there can be no face-to-face contact between an employee of a private collection agency and a taxpayer?

Mr. BROWN. That is right. The contacts are either done by mail or by phone.

Mr. CAMP. So, the only kinds of contacts we can have are either a letter in the mail or a phone call?

Mr. BROWN. That is correct.

Mr. CAMP. Now I presume that there are phone calls from private collection agencies where people verify that they are not that person. They have got the wrong number or—what happens then with the private collection company?

Mr. BROWN. That should be the end of it.

Mr. CAMP. Mr. Penaluna, do you want to comment?

Mr. PENALUNA. That is correct. Once the consumer identifies to stop calling or—they would not necessarily know what the debt was about because once they could not authenticate—once they actually tell us to stop calling, we will stop that and actually refer that back to the IRS.

Mr. CAMP. I presume phone numbers after 6 months get reassigned. A lot of your cases are 3 months old. So, I presume you are calling a lot of wrong numbers.

Mr. PENALUNA. That is correct. We have identified that about 15 percent are wrong numbers.

Mr. CAMP. At that point you stop contact when you discover that?

Mr. PENALUNA. Yes, sir.

Mr. CAMP. Thank you, Mr. Chairman.

Mr. LEVIN. [Presiding.] Mr. McDermott.

Mr. MCDERMOTT. Thank you, Mr. Chairman. I remember we sat through hearings listening to taxpayers that thought they were harassed by the IRS and we changed the law under the Repub-

licans. Now we have turned it all over to the private collectors, so now we have got to look at this.

Ms. Olson, I, first of all, I want to enter into the record a couple of faxes or mimeographs—I guess they are faxes of envelopes that look like junk mail. This kind of stuff comes in. It has a Telepark address in Waterloo, Iowa, and does not say anything on it. No one would open that. Throw it away immediately it looks like to me.

So, a part of the problem here is, that tax collector is not honest about what he is doing, I guess.

Mr. LEVIN. Without objection, that will be entered into the record.

[The information is being maintained in the Committee files.]

Mr. MCDERMOTT. Mr. Penaluna reported a miracle here, and I want you to tell me how this happened. It says over 20,000 IRS cases were handled by them. They received 55 complaints and none of them have been validated—I don't know what that means, "validated"—by the IRS or the Taxpayer Advocate Service.

Now, how could it be that there was not one single valid complaint on 20,000 contacts? Could you explain that process, what happens?

Ms. OLSON. Well, first, I would disagree that none of them are validated by the Taxpayer Advocate Service because we have 300 cases that came either from taxpayers calling—

Mr. MCDERMOTT. Are you saying that his testimony is incorrect?

Ms. OLSON. I am saying that we have seen many problems with this program through our cases. I don't know what ones are attributable to CBE and I can go back and find that out for you.

Mr. MCDERMOTT. Would you, please.

Ms. OLSON. Yes, sir. I can tell you that I have concerns about the complaint review process. I think the IRS takes a very narrow deposition of what complaints are and a even more narrow definition of what constitutes validation.

Second—

Mr. MCDERMOTT. Who is it that gets these complaints?

Ms. OLSON. Well, the complaints are referred by the PCAs to the IRS Private Debt Collection Program office. With the exception of an employee from my office, everyone who serves on that review panel are actually people who work on the Private Debt Collection Program and who are being evaluated by their supervisors for the success of that program.

Mr. MCDERMOTT. So, you are saying that the fox is handed the keys to the hen house, and they don't find any problems?

Ms. OLSON. I have tried to think about this. If you had a review board that actually had an EEO representative or an external civil rights unit representative, representatives of collection employees, on the board, you might have a more balanced perspective of what were the actual practices that we should be holding these PCAs to, what are the standards that we should be holding them to.

In fact, the review board views itself as a rubber stamp because it is the contract representatives, the COTRs, who are handling the contract that actually make the recommendations to the board, and in most instances, they are rubber-stamping what the COTRs say.

There have been instances where my representative has been outvoted on the board. We have felt that there has been a violation and we have been outvoted.

Mr. MCDERMOTT. Now, if somebody calls me up and says that they want my Social Security number, can you give me a valid reason why I shouldn't give it?

Ms. OLSON. I would never give it. I cannot give you a reason.

Mr. MCDERMOTT. Well, I mean, can they steal my identity if I give them my Social Security number?

Ms. OLSON. Yes, sir. They can steal your identity; they can if they have your address.

One thing that we have been talking about, that the IRS has been talking about is getting the private collection agency the birth dates of these taxpayers. So, if someone were to ask—a taxpayer gets a call and someone is asking them to verify their birth date, between your birth date and your Social Security and address you could create a whole identity and do a lot of damage to a person.

Mr. MCDERMOTT. Those records that these debt collectors—they are basically all secure in computers that can't be hacked and so forth?

Ms. OLSON. This is what the IRS says. In one of the PCAs the Treasury inspector general, in his most recent report, identified several security breaches. This is of some concern to me; I cite this in my testimony.

They found doors unlocked and file drawers unlocked. This is the PCA that the IRS terminated contract with, and that PCA is now able to keep our taxpayer files for 2 years and I have very many concerns about that.

Mr. BROWN. I have to correct that. The PCA that is no longer working on this has no IRS files at this point. Sorry to interrupt.

Mr. MCDERMOTT. So, is there any way to fix this law to give PCAs enough information so we don't have that kind of phone call that we just listened to?

Ms. OLSON. If you fix the law, then you are changing the Fair Debt Collection Practices Act, and many of those rules under the Fair Debt Collection Practices Act were put in to protect taxpayers from getting phone calls at their homes and offices saying, Hi, I am the debt collector and I am out to get you. I am calling from so-and-so.

So, you are in this double bind. The only solution is for the IRS to be collecting the taxes. That is where you have the protections.

I do want to go back to the placement of the files, whether they are the actual files or they are the electronic files. We verified with the IRS program office that these files were kept.

Mr. MCDERMOTT. I rest my case that the IRS are the only ones that can collect taxes without revealing—without invading people's privacy.

Ms. OLSON. I agree.

Chairman RANGEL. [Presiding.] Mr. Ramstad.

Mr. RAMSTAD. Thank you, Mr. Chairman.

Commissioner Brown, I want to get this straight. Did you say that in April, according to an IRS study, there was a 97 percent approval rating for PCA's efforts to collect delinquent taxes?

Mr. BROWN. It is not an IRS study; we contracted that out to a independent group.

Mr. RAMSTAD. It was an independent study. A similar result for IRS?

Mr. BROWN. The numbers are quite comparable.

Mr. RAMSTAD. It would seem to me that with a 97 percent approval rating for PCAs' efforts to collect delinquent taxes and with Congress' approval rating at 36 percent, maybe we can learn something.

Here we are bashing, based on a few anecdotal cases, a practice that promises to collect \$1.5 billion and \$2.2 billion for the taxpayers, money that would otherwise go uncollected; and we are taking a couple anecdotal cases—and perhaps there have been some abuses, certainly some alleged abuses—and people want to trash the law. It makes no sense whatsoever if you are pragmatic at all.

Mr. Penaluna, I think you should make Ms. Benoit, based on what we heard here today, employee of the year. She personified patience and courtesy in responding to the gentleman.

But more seriously, let me ask you this: It is because of taxpayer confidentiality laws, isn't it, that the caller we heard was not told that his call concerned a tax debt?

Mr. PENALUNA. Yes, that is correct.

Mr. RAMSTAD. The privacy laws preclude that?

Mr. PENALUNA. The privacy laws and the fact that we only have the Social Security number for the authentication.

Mr. RAMSTAD. Commissioner Brown, I would like to ask you a question. Is it true that the IRS does not provide the private collect agencies with the last known phone number of the taxpayer, even if the number is available?

Mr. BROWN. Because the accounts are, on average, about 3 years old, we just did not think the numbers would be current. Now that GAO has looked at this, we are going to study the recommendation quite closely here.

Mr. RAMSTAD. Well, if, as implied by Ms. Kelley, it is so easy for the IRS to set up an outbound call system, why hasn't the IRS done so in the past?

Mr. BROWN. Well, we do conduct some outbound calling, and actually we do some in the site.

I will say that the vast majority of our calls are inbound; because of the tools we have when we talk about a lien or a levy, people tend to call us.

Mr. RAMSTAD. I want to thank all the witnesses here today. It reinforces my view as everybody here thinks—agrees, close the tax gap. With a program, the PCA program, over the next 10 years, it is projected to collect \$2.2 billion in unpaid delinquent taxes, money that would otherwise go uncollected.

That point needs to be reemphasized. I think it would be absolutely foolhardy to do away with this practice, and I commend the good work that you are doing. We are proving this is not an exclusive function of the government, as many, many other agencies have proven in the past.

I yield back, Mr. Chairman.

Chairman RANGEL. Mr. Neal.

Mr. NEAL. Thank you, Mr. Chairman.

Ms. Olson, we have just heard that these phone calls typically start off with a request for a Social Security number and the taxpayer cannot find out anything more about these repeated phone calls until that number is divulged. I have a document from the Social Security government Web site that warns us that we should not divulge this number to private businesses unless we understand what law requires us to give it to them, because as the Social Security Administration states here, and I quote, "Only the IRS can request this for the purpose of tax returns."

Ms. Olson, at the risk of being redundant, do you think these taxpayers should be divulging Social Security numbers over the phone?

Ms. OLSON. No, I do not.

Mr. NEAL. Mr. Brown, do you think they should be divulging their Social Security numbers?

I want you to picture for a second perhaps a couple of 90-year-old citizens. Do you think that they should be asked to give this information out over the phone? I wouldn't tell my children to give it out over the phone, let alone my 90-year-old neighbors or parents.

Mr. BROWN. I think when you place this in context, and they have received four notices from the IRS, a letter from the IRS explaining that the case is now going to be assigned to a private debt collector, a letter from a private debt collector saying we are going to be calling you soon, we have been assigned your case, it is not much of a surprise when a phone call occurs.

Mr. NEAL. Ms. Olson.

Ms. OLSON. Mr. Brown has said already that these cases are 3 years old. The four letters come immediately very early in the collection stream. If somebody files a return with a balance due, the four letters come at that point. So, it could be 2 years ago that these letters were sent out to them, the letter that comes to the taxpayer telling the taxpayer that the PCS is going to be writing them.

Of the \$19.5 million that was collected under this initiative since September, 4 million of those dollars, 20 percent, came from the IRS sending a letter. So, for the price of a postage stamp, people were sending us money without any contact whatsoever. We could continue to do that, not jeopardize identity, not jeopardize Social Security numbers.

Mr. NEAL. Mr. Brown, how many letters are returned to you from the Postal Service?

Mr. BROWN. I don't know, I will have to find an answer out for you.

Mr. NEAL. Do you have somebody on the staff there that might be able to tell you that?

Ms. OLSON. Congressman Neal, we did a—

Mr. BROWN. Five thousand.

Mr. NEAL. Five thousand. Thank you.

Ms. OLSON. We did a study with the earned income credit population where we found that about 30 percent, 25 to 30 percent of taxpayers within 6 months of filing their return had moved and most of them had left no forwarding address.

So we have a population that moves around a lot. Many of these letters do not—are not received by taxpayers.

Mr. NEAL. Mr. Brown, back to you. Perhaps that citizen served honorably in World War II, has paid their taxes all of their lives and maybe are suffering from a case of dementia, early stages, or suffering from Alzheimer's.

Is it still your position that they should give out Social Security numbers to somebody on the phone who won't identify themselves?

Mr. BROWN. I point out that they can opt out of this program at any time they want.

Mr. NEAL. At 92 or 93 years old, what do they do?

Mr. BROWN. If they are concerned at all about the interaction, there is a phone number. They can call the Internal Revenue Service. All they have to do is tell the private debt collector on the phone that they don't want to work with them. The case would be reassigned to the IRS.

Mr. NEAL. Do you think that is easily accomplished for an individual at that age?

Mr. BROWN. I can't speak to that, sir.

Mr. NEAL. Let me give you a suggestion, because most of the Members of Congress, we spend a lot of time at senior centers. Maybe you ought to go out and try that. I think that is a piece of good advice.

Mr. Kutz, let me understand your testimony regarding the survey. Did you say that only 1,000 taxpayers out of hundreds of thousands in conversations completed the survey, and if so, does that seem like a statistically valid sample?

Mr. KUTZ. The sample was not statistically valid because not all people were offered the survey, so—you can have a small number respond and project it to a large population. But the reason that there was a problem here was because of the methodology that two of the three private collection agencies used. So, not everyone who actually agreed to take the survey took it.

Mr. NEAL. Commissioner Brown, is it your position that this 94 percent satisfaction rate, even based upon the testimony of Mr. Kutz, do you think this is at all valid?

Mr. BROWN. In April, the survey was offered to all taxpayers.

Mr. NEAL. Mr. Kutz, do you want—

Mr. KUTZ. It wasn't all taxpayers; it was all right-party contact. The telephone call that you heard there, that person did not validate their identity. Anyone who was called that did not validate their identity was not part of this survey.

I think the results need to be limited to the right-party contacts or people who authenticated they were part of the 3,000 cases referred, so that would overstate the survey results. It needs to be limited to who authenticated they were the taxpayer involved here.

Mr. NEAL. Mr. Brown, last, a piece of advice that we have had in my household for many years. I instructed my children, don't give out any personal information over the phone. I think you have to take that into consideration now.

Mr. BROWN. Yes, sir.

Mr. NEAL. Thank you.

Chairman RANGEL. Mr. Brady.

Mr. BRADY. Thank you, Mr. Chairman. I would like to yield to the Ranking Member, Mr. McCrery.

Mr. MCCRERY. Thank you, Mr. Brady.

I am concerned about this issue of the Social Security number. But as I understand it, the private debt collectors have to verify the identity of the person they are calling with the Social Security number, otherwise they violate the Privacy Act. So, it is a Catch-22 here.

But the IRS, when the IRS calls, they can say to the person, This is the IRS and give us your Social Security number. Is this number 433-blah-blah-blah? The guy says, Yes.

Why can't we authorize, through statute, the private debt collectors to say, This is CBE Company calling on behalf of the IRS, so that they then know what the subject is, and it is the same thing as if the IRS were calling? It seems to me that would solve—it would put the private debt collectors in the same standing as the IRS in terms of getting the information they need to verify the identity. Otherwise we are going to continue to have this problem.

I agree, if somebody called me and said, What is your Social Security number, I would say, Buzz off; that is my business.

So, maybe that is a problem. That is a problem, but it seems to me it is not a problem that can't be fixed. We ought to be able to fix that. But I think we have to do it by statute in order to assure private debt collectors they wouldn't be in violation of the Privacy Act.

Thank you, Mr. Brady.

Mr. BRADY. Thank you. I think when it comes to taxpayer rights, you can't be too careful.

I think that this hearing is premature in evaluating the success of this program. We are told that there are many, many violations of this program, but I don't believe that is true. We have not seen complaints in our offices. Out of 37,000 cases, there have been 69 with concerns and only a few, 25, about the taxpayer treatment. That is a pretty strong record.

I want to point out, too, that of the firm whose contract IRS did not renew, two of the three violations were self-reported by the company. They identified the problem and, by contract, told the IRS. That is exactly what they are supposed to do, and then correct it.

We are told that these are easy collections, but that is not accurate either. Over 2 or 3 years with multiple contacts, they are still not collected. If these were easy collections, why didn't the IRS collect them themselves during that period?

We are told that tax collection is a core function of the government. I don't believe it is. I think efficient and complete tax collection is the core goal of our government, and I think that the private companies can be helpful. They have a track record both at the local level—in our communities most of our property tax collections are done through private agencies at the State level; more than half have private agencies collecting their income taxes. I think the Federal Government, which is always slow and tends to trail the States when it comes to solving problems, has an opportunity to sort of learn from those successful programs and apply it to ours.

I think—and I will wrap up with this. Mr. McCrery asked my question, but I think it is premature to kill this program. I think we need the balance of the IRS' strengths, and the IRS employees, who are very good at what they do, complemented with the expertise of the private agencies who can handle some of the areas that IRS perhaps could use some help with.

I think that at this point we need to work on improving the program, always safeguard taxpayers' rights, but keep our eye on the goal of efficient and complete collection of as much of our taxes as we can.

I yield back, Mr. Chairman.

Chairman RANGEL. Mr. Becerra.

Mr. BECERRA. Thank you, Mr. Chairman.

Let me ask one preliminary question, and perhaps, Mr. Brown or Ms. Olson, you could answer this. Is it accurate to say that most of this private debt collection occurring for the IRS involves taxpayers who are middle-to-lower income Americans? So,—less than \$70,000 or so that you consider part of middle America?

If I could get a quick "yes" or "no" or you will have to get back to me, I have a lot of other questions.

Ms. OLSON. The IRS does not select cases based on income. They look at level of debt. Most of the cases involve very small debt, about \$5,000 in debt. Our office pulled from IRS data and found that the population of cases going out to the PCAs were disproportionate—had a greater proportion of earned income credit cases, taxpayers who had claimed the earned income tax credit.

Mr. BECERRA. Which are taxpayers below \$40—or \$45,000?

Ms. OLSON. Yes. The adjusted gross income for those taxpayers was lower than the IRS population as a whole.

Mr. BROWN. I would have to disagree with that assessment of the numbers. The numbers are identical for our automated collection program as they are for the private debt collection.

Mr. BECERRA. We are still in the main looking at folks in this program that have incomes of, say, less than 100,000?

Mr. BROWN. When we do collection work, we don't look to see how much money the taxpayer earns.

Mr. BECERRA. Is it possible to find out?

Mr. BROWN. Yes.

Mr. BECERRA. Can you do that for us, Mr. Brown?

Mr. BROWN. Yes.

[The information is being maintained in the Committee files.]

Mr. BECERRA. Appreciate that.

Mr. Penaluna, let me ask you a question. You are the president of this company that does some of the debt collection. Do you give out your Social Security number to anyone over the phone who is a stranger to you?

Mr. PENALUNA. No, sir.

Mr. BECERRA. We have heard about identity theft cases where people will collect one bit of information or two bits of private information on an individual and then try to do something to confirm that those two bits of information correlate to the third bit of information. With that, bingo, they are now able to go ahead and do whatever they want to with your private information as they wish.

Would you advise any American to disclose any kind of private identifying information to a stranger over the phone?

Mr. PENALUNA. It depends under the circumstances. In the case of this program—

Mr. BECERRA. So, it depends on the circumstances? Then I gather that the answer is "yes."

Mr. BROWN. Under certain circumstances.

Mr. BECERRA. I have 5 minutes. I am trying to figure out—if there are circumstances, I will try to find out about them. But I am trying to figure out if under any circumstances you would advise Americans to provide their private information to a stranger over the phone.

Mr. PENALUNA. There are some circumstances.

Mr. BECERRA. Okay. Would you also under any circumstance advise any American to confirm private information over the phone where, as an example—as we saw in this case here that was played for us, where someone was saying, Will you at least tell me if this is your correct Social Security number or this is your correct address or this is your correct driver's license number—are there any circumstances under which you would advise an American to confirm that private information?

Mr. PENALUNA. Under certain circumstances.

Mr. BECERRA. Mr. Brown, on the survey, I am troubled that you—IRS continues to rely on this survey of 94 percent overall satisfaction. Let me make sure I understand this.

There were 35,000 taxpayers who owed taxes that were targeted. We are given the information that over 300,000 contacts were attempted by these private debt collectors to collect on the 35,000 people. Actually, over a million contacts were attempted and over 300,000 Americans were approached to try to find the 35,000 universe of taxpayers who owed money, correct?

You are saying there is 94 percent overall satisfaction.

As we heard Mr. Kutz say, that relied on a survey provided by the debt collectors to come up with that number. So, when you say 94 percent overall satisfaction, you are not saying 94 percent of the 300,000 Americans who were contacted are satisfied, are you?

Mr. BROWN. No.

Mr. BECERRA. Because that would be over 280,000 Americans who would have said, Yes, we are satisfied with the work done by these private debt collectors.

Mr. BROWN. No. As Mr. Kutz explained, we were talking about the people were verified as the taxpayer.

Mr. BECERRA. I am looking at a chart, and I came up with a total of fewer than 2,500 people who were contacted.

I believe, Mr. Kutz, you said it was something around 1,000?

Mr. KUTZ. It was 1,011 people.

Mr. BECERRA. From that 1,011 people you extrapolate 300,000 Americans, 94 percent of them were satisfied with the work that was done through the private debt collectors.

Mr. BROWN. I am extrapolating that the people who were contacted were happy with the interaction.

Mr. BECERRA. The contacts—and I will close with this because my time has expired—of the folks who were contacted and then the small universe that was used to come up with the survey, IRS did

not choose who those people would be who would submit the survey results, were they?

Mr. BROWN. That is correct. We did not.

Mr. BECERRA. All the people who were contacted were asked, will you submit a survey?

Mr. BROWN. Yes, they are offered it at the end of the phone call.

Mr. BECERRA. Let me rephrase.

All the people who submitted a survey, those that were forwarded to the IRS for purposes of determining the survey results, all of those people forwarded were forwarded by the tax collectors themselves?

Mr. BROWN. No. By an independent consulting group.

Mr. BECERRA. The independent consulting group got those results from whom?

Mr. BROWN. The caller is referred at the end of the phone call to an independent consulting group.

Mr. BECERRA. Who does the referral?

Mr. BROWN. The private debt collector.

Mr. BECERRA. Do you know that the private debt collector—of the people that were contacted—gave that information to the American to make the call to that survey collector?

Mr. BROWN. At the end of every call where you have talked to the taxpayer, they are required to send them along to the survey if they wish to take it.

Mr. BECERRA. Thank you, Mr. Chairman. My point there is that, again, it is a very selective survey that is the result.

Mr. Chairman, just for the record, I wanted to ask Ms. Olson some questions, because all of her testimony is based on our request to get back to us. So, I had some questions for Ms. Olson which I will probably put in writing.

But I thank you for having responded to our requests with your testimony today, as the result of our request that you do so.

Ms. OLSON. You are welcome.

[The information is being maintained in the Committee files.]

Chairman RANGEL. Mr. Reynolds.

Mr. REYNOLDS. Thank you, Mr. Chairman. This hearing is kind of a big day for western New York. We are fortunate to have Ms. Paray from Cheektowaga in western New York; and we are privileged also to have the president and some representatives of Pioneer Credit Recovery, who have 1,200 to 1,400 employees in western New York; and of course, four members from New York on the Committee on Ways and Means chaired by a New Yorker in Chairman Rangel.

As I see, first, how we got into the collection business, it was tax gap means, can we close it and can we use legitimate means to get there? One of those was to use PCAs, which ended up with an opportunity that GAO says is \$1 billion minimum over 10 years of revenue. Of course, in our world now with PAYGO, that is pretty serious in how we meet being able to close the tax gap but also not incur additional expense.

As I kind of look at this, having western New Yorkers so integrally involved, some of this seems to me that we have got a view, can public employees that are also represented by their union, can they do a better job? Or can private collectors do a better job or

can they do an equal job? How do we just plain get that \$1 billion over 10 years?

My first question, Ms. Olson, could you just again tell me the mission or the purpose of the National Taxpayers Advocate's office?

Ms. OLSON. Sir, my mission is in 7803(c) of the Internal Revenue Code where Congress instructed me to help taxpayers solve their problems with the IRS, to identify administrative and legislative means to mitigate those problems.

I make an annual report to Congress—actually twice a year, but in my December report, I identified private debt collection as a more serious problem for taxpayers. In doing that, I looked at the need to collect the tax gap and the best way to collect the tax gap.

One of my concerns was that IRS employees, in collection their primary mission is sort of the three Cs: to do cause—what caused the taxpayer to have this problem? How do we cure it? How do we bring the taxpayer into compliance?

The private debt collectors, their mission is simply to collect the tax. They don't get into questions about, do you owe the tax, if the taxpayer does not believe they owe the tax; or being able to do a settlement for it rather than full pay, because that is what the taxpayer needs in order to continue to pay taxes and be in compliance.

That is really a big difference, sir.

Mr. REYNOLDS. Thank you. Could you tell me how many employees you have?

Ms. OLSON. I have 1,900 employees around the country.

Mr. REYNOLDS. Of the 1,900 employees, how many are covered by union contract?

Ms. OLSON. Maybe about 1,600 are bargaining unit.

Mr. REYNOLDS. Thank you.

Could I get from Mr. Kutz: Do you believe that the study that was commissioned was a bona fide result as you got that data back that you cited in your testimony?

Mr. KUTZ. The study being the survey? Are you talking about the taxpayer survey?

Mr. REYNOLDS. Yes.

Mr. KUTZ. No, not for the period we looked at. I believe there are some methodological issues that we understand have been corrected, starting early April, with respect to offering everyone the survey.

I think everything that has been discussed here is that the survey should be qualified only to those people who authenticated their identity, and any of those who did not authenticate their identity were not included in any survey.

Mr. REYNOLDS. Out of curiosity, is there any way that you might have known—we have, and I will submit for the record again the Inspector General's audit on the laptop computers that were lost and the press that accompanied that.

Are you aware of any lost data by the PCAs that have come to your attention relative to taxpayers?

Mr. KUTZ. That wasn't something that we looked at.

Mr. REYNOLDS. Who would look at that?

Mr. Brown?

Mr. BROWN. Yes, we would.

Mr. REYNOLDS. What you have found?

Mr. BROWN. You are talking about losing hardware, specific laptops?

Mr. REYNOLDS. As you know, the Inspector General did an audit on the IRS and there were lost laptops that were published in the national news. Are you aware of any lost data similar to what the Inspector General found in the possession of the PCAs?

Mr. BROWN. No, we are not aware of any losses.

Mr. REYNOLDS. Just if I might from the gentleman from Iowa, Mr. Penaluna, I have had occasion to visit the Pioneer Credit Recovery in my district and so I know a couple of things: one, the extensive training; two, the additional work that they require of their employees, and the fact that my own tax counsel who works on Ways and Means wasn't even admitted physically to see the site that was done for the IRS.

Could you review some of the safeguards or the conditions the IRS set forth that you must meet in order to do your job and still meet an 18.5 percent revenue base?

Mr. PENALUNA. Yes, sir, it basically falls into three areas. It is covered by staff, facilities and our systems.

In the case of our staff, all of our staff are experienced employees who go through at least a 3-week training on IRS policies and procedures. They go through a full Federal security background check, fingerprinting. They actually sign all the forms and fall under all the same guidelines that any Federal IRS employee would.

In regards to our facilities, our facilities have to be independent from the rest of our facility.

In the case of our company—pardon me, sir?

Chairman RANGEL. Could you describe the circumstances? He has run out of time.

Mr. PENALUNA. The facilities is the second one, that they have to be secure.

The third one are our systems; our systems have been authorized by the IRS and meet all of those requirements.

All three have to be approved to be able to handle the contract.

Chairman RANGEL. I thank the gentleman. The gentleman's time has expired.

Mr. Blumenauer.

Mr. BLUMENAUER. Thank you, Mr. Chairman. I was interested, the 3 weeks' training in IRS procedures. I wonder, Ms. Kelley or Ms. Olson, if you could contrast the 3-week training on IRS procedures with the thousands of professionals that we have in the IRS now who do this in other regards.

Ms. OLSON. I will certainly let our revenue officer, an ACS employee, talk about the training that she gets.

But IRS employees every year get training on confidentiality, unauthorized disclosures. It is repetitive. Collection employees every single year get training in different modules that emphasize the importance of taxpayer rights, as opposed to 20 minutes that private collection agencies get on confidentiality, or 20 minutes on taxpayer rights and a 2-hour video that my office insisted on it being prepared, so that we had some assurance that the PCA employees understood the key nature and the unique nature of tax issues.

Mr. BLUMENAUER. Ms. Kelley, part of what is in the back of my mind is what we now know to be sort of trumped up and overblown series of hearings that led to really eviscerating the IRS' capacity. A couple of isolated incidents trumped up and blown out of proportion as opposed to the day-in-day-out service that we receive.

Could you help us get the context here of what the people you represent, the professionalism and how it relates to some of what we have heard here today?

Ms. KELLEY. Sure. The employees that do this work on the telephone, the same kind of work turned over to the PCAs, I believe their training program is an 8-week classroom training and 3 weeks of on-the-job training. Liz could speak a little more to that.

In addition to these annual trainings around taxpayer rights, which is, first and foremost, as important as collecting the taxes to IRS employees—and their job, also—the training also goes to what I mentioned in my testimony, that this is hopefully not about a taxpayer having a tax debt year after year. The employees who do this collection work in the IRS work with the taxpayer to help them be a compliant taxpayer in the future—to educate them, to give them information, to answer questions, to help put them on a track to get off of the list of delinquent taxpayers. That is part of what all of this training and the obligation of IRS employees is about.

Mr. BLUMENAUER. Thank you.

I am also interested in the notion of the return to the taxpayer. There is nothing inherent—I appreciate, Ms. Olson, in your testimony and also, Ms. Kelley, in what you very extensively put forth, there are alternatives to raise not just this money, but far more money if we are willing to make the investment; and that there are actually strategies that we could undertake that would be in compliance with our sometimes perverse budgetary rules that end up costing money to save money.

But there are techniques that would end up having a much greater rate of return. Would either of you just comment on that?

Ms. OLSON. Well, in my annual report this year I discussed IRS' collection strategy and critiqued it rather, I believe, thoroughly to point out that there are many things that the IRS could do with the resources that it has right now for us to be able to touch the taxpayers that the PCAs are working on, as well as doing other work.

I think we need to make more outbound calls. We need to use greater resources to locate taxpayers. We don't do half of what we could do to find taxpayers and send letters to them.

Mr. BLUMENAUER. My time is up. There are others who have waited patiently.

Mr. Chairman, I am intrigued with the testimony that we have received here, that there are discrete, concrete steps that we can take to make sure that we are collecting all of the money that is talked about here and far more at far less cost to the taxpayer. I would look forward to working with you and the staff to find mechanisms that we could use, without falling prey to our budget rules, to be able to give these folks the tools they need to help our taxpayers and get the money that the Treasury is owed.

Thank you very much.

Chairman RANGEL. Mr. Brown, do you think we could have a moratorium on new contracts until the Committee and your staff have an opportunity to try to perfect some of the problems that we are having with these contracts?

Mr. BROWN. The contract is set to expire next March, if we don't take steps very soon to put this out for bids. Our plan is to put it out for bids in June and to award contracts in October.

Chairman RANGEL. How can we try to improve what is going on here, rather than have us legislate, which I think would be costly if we had to do that; can't we work out something?

Mr. BROWN. I think the ranking member has made a suggestion which I find persuasive. One of the problems in the authentication process is that the debt collectors can't say that they are calling on behalf of the Internal Revenue Service.

Chairman RANGEL. I am talking about the new bids out there. What happens if you delay them?

Mr. BROWN. The program will terminate in March.

Chairman RANGEL. We have to talk. Because we don't want to superimpose our judgment on you, but we have to find some way that we can work together rather than just legislate that you don't do it.

So, let's see what we can do after the hearings and see if we can work out something.

Mr. Doggett.

Mr. DOGGETT. Thank you, Mr. Chairman. While the focus this morning is appropriately on debt collection, the overall theme is the privatization of primary functions of the Internal Revenue Service. Commissioner Brown, I would like to explore with you one of the other areas that, for the first time in history, appears to have been outsourced by the Service; and that is, IRS noticed 2007-17 concerning real estate mortgage investments and the decision of the Internal Revenue Service to turn over to those accountants and lawyers, whose job is to minimize taxes paid by their clients and avoid as many taxes as possible, the job of preparing the first draft of the regulations that the Internal Revenue Service would promulgate.

Are you familiar with that?

Mr. BROWN. I am.

Mr. DOGGETT. You set an April 30th deadline.

First—while IRS has, of course, hired technical experts to provide advice in the past, this is the first time in the history of the Service where you have actually said what some might characterize as asking, not the fox to guard the hen house, but the fox to design the hen house, and draw up the regulations for these complex real estate transactions.

Mr. BROWN. Our chief counsel actually is here, and this resides in the chief counsel's organization.

Mr. DOGGETT. I am glad for him to respond as well.

Mr. BROWN. Let me start. I think the analogy is not apt. What we are talking about here is getting input from people who are affected by the guidance.

Mr. DOGGETT. Well, you have had a mechanism to do that since the Service was first formed, the same mechanism that is available to every Federal agency to post its proposed regulations, proceed

with rulemaking under the Administrative Procedure Act, and get comments from all affected, don't you?

Mr. BROWN. That is correct.

Mr. DOGGETT. So, it is highly unusual, indeed historic for the Commission to say, well, what we really need to do is just ask these tax lawyers and accountants to draw up the regulation.

Mr. BROWN. They are not actually going to draw up the regulation.

Mr. DOGGETT. They are going to make proposals and first drafts, aren't they?

Mr. BROWN. As they do now.

Mr. DOGGETT. They offer comments after the IRS has proposed a first draft?

Mr. BROWN. No, the process works a little bit differently.

When we announce in a published guidance plan that we are going to be taking a look at something, a lot of people start to write in right then.

Mr. DOGGETT. Well, of course. Indeed, a tax practitioner at the local level, not someone here in Washington, can offer a suggestion at any point to the Service for a regulation that they are either contemplating or not contemplating. I suppose; isn't that right?

Mr. BROWN. That is correct.

Mr. DOGGETT. But it is unusual to announce you are working in a particular area without proposing the regulation and inviting those who are regulated, and their attorneys and accountants, to propose the regulation.

Mr. BROWN. Well, I think we generally tend to hear from the people who are most interested in the subject.

Mr. DOGGETT. Undoubtedly.

Mr. BROWN. We typically hear from them very quickly.

Mr. DOGGETT. In this case you asked them to start the process.

Mr. BROWN. In a select number of instances.

Mr. DOGGETT. In fact, it is called a pilot program; and my concern is, if this pilot works like most pilots in government, the idea is to turn over the job of preparing the first draft of regulations in other complex tax areas that have been the subject of tax shelters and tax avoidance in the past to the private sectors.

Mr. BROWN. There are no such plans, but we would be happy to come up and give a full briefing and have the chief counsel come up and explain exactly what is contemplated here.

Mr. DOGGETT. You mean, if you are not satisfied with this process, you don't plan to ever use it again, even though you are satisfied with it?

Mr. BROWN. No. Generally, the whole point of a pilot is to see if it works.

Mr. DOGGETT. That is my concern, that if IRS, with its move to privatization of primary functions, decides that this one works, that we will see it in other areas that have been the subject of tax avoidance.

Do you agree with the comments that were made by the various experts that were quoted in the New York Times that there is an advantage to be had if you drew the regulation initially, if you offered the draft that the Service accepts?

Mr. BROWN. No, I don't agree with that. If in the end, we get all kinds of submissions from the private sector and from government entities about things we are talking about issuing guidance in. Some of them are quite persuasive; others quite frankly, are not worth the paper they are printed on.

Mr. DOGGETT. What has happened in the process since April 30th, I believe when the proposals were to be submitted? What is the plan now for how you are going to proceed on this?

Mr. BROWN. We have gotten three responses. We are evaluating them right now, and we are making sure this process is as transparent as possible.

Chairman RANGEL. The time of the gentleman has expired.

Mr. Linder.

Mr. LINDER. Thank you, Mr. Chairman.

Mr. Penaluna, Ms. Benoit, after 1 minute in the phone call, told the taxpayer that he understood and she would mark up his chart. He kept her on the phone for the next 4 or 5 minutes.

If you were making a call, wouldn't you get suspicious about that call?

Mr. PENALUNA. Yes, sir.

Mr. LINDER. Don't you think she was suspicious she was being taped?

Mr. PENALUNA. We tape all of our phone calls. None of our employees have a suspicion they are being taped; they know they are being taped.

Mr. LINDER. That tape was coming from the taxpayer, wasn't it?

Mr. PENALUNA. That tape came from us.

Mr. LINDER. Ms. Olson, you said that you get 20 to 1 return on every dollar. Ms. Kelley said it was 13 to 1. Which is correct?

Ms. OLSON. Mr. Brown actually said 13 to 1.

Mr. LINDER. Ms. Kelley did, too.

Ms. OLSON. Okay. Their number is based on startup costs that came from IRS research. Our data came from actual data from the IRS for the ACS program. A GS-8, step 5, ACS; that is, the midgrade of the step of the GS-8 level is about—

Mr. LINDER. Thank you. You have been quite concerned about this sample script that inserted the phrase "psychological pause." What if the script said "wait for an answer?"

Ms. OLSON. If it said "wait for an answer" and it did not say "the next person who speaks loses," it might not raise concerns.

Mr. LINDER. What is the difference?

Ms. OLSON. When your message is saying the next person who speaks loses, you have turned debt collection into a game, and it is a power play.

Mr. LINDER. Having been collected for debt myself and audited, it wasn't a game to me, but it was pretty brutal for a no-change audit. You are expressing your concerns about security breaches on behalf of the taxpayer that you advocate for. But you did not express any concerns about the 490 computers that disappeared from the IRS, 44 percent of which had unencrypted sensitive data, including taxpayer data.

Ms. OLSON. Sir, that is not correct. I do express concerns about that. I have sent messages out to my own employees, if they have a laptop, how they are to take care of their laptop.

Mr. LINDER. Did any of those computers come from your employees?

Ms. OLSON. I believe some of them may have.

Mr. LINDER. Ms. Kelley, you represent the union; is that correct?

Ms. KELLEY. Yes, I do.

Mr. LINDER. During the past year, over 100 IRS employees have been removed, resigned, or retired because they either failed to file their tax returns or they understated their Federal tax liability.

Do you have any comparable statistics for private collection employees?

Ms. KELLEY. I don't, because that number is not available.

That number is collected on Federal employees and on congressional staff as well, actually.

Mr. LINDER. Does that concern you?

Ms. KELLEY. Well, it concerns me for a number of different reasons than probably what you would suggest.

First, I think everyone should pay their taxes and I think that IRS employees know that they are held to a higher standard. No other employee in the public or private sector will lose their job for not paying their taxes or paying them on time. They are held to a higher standard.

But I also know that many of those employees who were fired are employees who do not do tax compliance work for the—they are clerical or administrative.

Mr. LINDER. Thank you.

Ms. Kelley, is it true—I want to get to Mr. Blumenauer's concern about return to taxpayers. Isn't it true there are 300 full-time equivalent employees who are paid by the IRS to do work for the National Treasury Employees Union? When you include the value of the benefits, the cost to the taxpayers is about 150,000 per.

If your ratio of 13 to 1 is correct, that opportunity cost is about \$585 million a year. Does that concern you?

Ms. KELLEY. I have not done the math, as you have done them, and it does not concern me.

Here is what does concern me.

Mr. LINDER. The taxpayers are paying to support and run your union and do the work for you, and—

Ms. KELLEY. Taxpayers are not paying to run our union, with all due respect. We have a statutory responsibility and obligation to represent the employees who elected the union. That is in statute. It recognizes that that is good for the country and good for the agency.

Management approves all the time that is spent on NTEU business by NTEU representatives. So, if there are issues, they have a right to deal with those; and we have the right to be accountable, and we are.

Mr. LINDER. Thank you.

Chairman RANGEL. Mr. Pascrell.

Mr. PASCRELL. Thank you, Mr. Chairman.

Mr. Chairman, I am very much disturbed by the Pioneer Credit Recovery sheet, for those who are making the calls for private collection. If I go down to the middle of the questionnaire after—once all the information is obtained, the following is written: "Okay"—the taxpayer's name—" based on the information you provide me, it appears you may be able to borrow the money to pay this past-due obligation."

Then, "Instruction: Give the taxpayer some ideas on how to borrow. Use the information from the financial statement."

Before I ask my question of you, Mr. Penaluna, I want to ask a question of Ms. Olson.

Ms. Olson, isn't it true that the IRS employee is trained to give counseling to the taxpayer, to find out what the cause of the problem is so that it does not occur in the future?

Ms. OLSON. Yes.

Mr. PASCRELL. Now, why is that done specifically, do you think?

Ms. OLSON. Because we are the government and we want taxpayers to continue to be in compliance. Having a taxpayer in compliance is the cheapest way to address a problem. It is ongoing if they become incompliant.

Mr. PASCRELL. We have concluded from what many of you have said on the panel that the IRS can do it cheaper and we have also concluded that the IRS needs more resources to do its job.

Ms. OLSON. Yes.

Mr. PASCRELL. If you had more resources, it still would be cheaper and the return would be greater; is that correct?

Ms. OLSON. Yes, it is.

Mr. PASCRELL. Mr. Penaluna, I want you to give me your impression of what I read from the form of Pioneer Credit Recovery. I want you to tell me how that struck you, or if it did at all.

Mr. PENALUNA. First of all, that is not our company's form.

But my response to that is, most of these taxpayers that we can authenticate usually have some kind of financial problems to begin with. So, we try to work with them to offer them possibilities of how they could pay their tax debt.

Mr. PASCRELL. You are also in the business of not only working for the IRS; you are a private contractor. But are you also in the business of providing the possibility in many areas—because you go through a number of these in this particular form that I am looking at—of how you might borrow your money, sir or miss, in order for you to pay or begin to pay your debt to the Federal Government; is that correct?

Mr. PENALUNA. Amongst other things, yes.

Mr. PASCRELL. There is the possibility you will loan them money to pay this off?

Mr. PENALUNA. We do not loan them the money. We provide them with financial resources.

Mr. PASCRELL. That is correct. That is correct.

Now, from the Committee's investigation of the private firms that have been contracted by IRS, they have concluded that the Private Debt Collection Program targets low-income taxpayers. They did not dream this up. The IRS claims it does not know the

income levels of taxpayer cases sent to private collectors. That is what their claim is.

[12:29 p.m.]

Mr. PASCRELL. However, planning data which the Committee is investigating indicates that 70 percent of the taxpayers had incomes of \$50,000 or less. I put the two things together and it would seem, I would conclude, that we are placing the collectors in a very particular position, maybe a procuring position. I mean, not only trying to get the dollars that are owed to the Federal Government, but also to loan the taxpayer the money to pay it off at whatever interest. I am sure they are not going to do it for nothing, are they Mr. Penaluna?

Mr. PENALUNA. I would not imagine.

Mr. PASCRELL. Thank you. I want to go on now, if I may.

What costs, Ms. Olson, is the IRS incurring as a result of transferring this work over to the private collection agencies? Monitoring their progress, including the lost opportunity, of course, the cost of employees working with the collection agencies instead of collecting taxes, what is the cost to the IRS?

Ms. OLSON. The IRS has said it is \$71 million.

Chairman RANGEL. Yes, could you submit that answer in writing to Mr. Pascrell?

[The information is being maintained in the Committee files.]

Mr. Pomeroy, please.

Mr. POMEROY. Thank you, Mr. Chairman. I will follow up immediately on the questioning offered—or the line of questioning being pursued by Mr. Pascrell.

Ms. Olson, would you provide the number? The question was, how much does this cost the IRS to get this going? Your answer?

Ms. OLSON. It is \$71 million through fiscal year 2007, the IRS projects.

Mr. POMEROY. Seventy-one million dollars. I would like to introduce into the Committee record testimony elicited at a hearing 4 years almost to the day, May 13, 2003, before the Oversight Committee. As this concept was being rolled out in this particular hearing, you have then-Commissioner Everson, who testified to our Committee: My understanding is that this would require an additional incremental investment now, something \$10 to \$15 million to develop a system because we would have to work very carefully with the PCAs in terms of the data they would gather.

I want us to contemplate, we thought this was going to cost us \$10 to \$15 million, commissioner's testimony. We have now spent \$71 million. I suggested at the time that going through private contractors as opposed to staff employees, this was like building the \$600 toilet seat in debt collection, the most expensive, least efficient way to do it. Certainly having a startup figure come in, a multiple of what was advertised by the Commission, would certainly raise some question about this whole thing. So, let's look at what we are netting, all right, how much are we bringing in? Commissioner, how much are we bringing in?

Mr. BROWN. Over the next 10 years it will be \$1.5 to \$2.2 billion.

Mr. POMEROY. That is not what I asked you. How much are we bringing in so far?

Mr. BROWN. Approximately \$20 million a year to date.

Mr. POMEROY. Seventy-one million dollars out, \$20 million in.

Mr. BROWN. We would note the program will break even next spring and be profitable.

Mr. POMEROY. The program will break even next spring. We are going to lose money on this darn thing for a couple of years, and then we may make a little in the outyears, although your projections so far haven't been worth a heck of a lot to this Committee on this matter.

Commissioner, do you have any notion of what we might have received if we had taken that \$71 million and instead of taking it from the IRS, from public resources to private vendors, what we would have done if we had staffed up and gone after this owed debt? Do you have any estimate in terms of what \$71 million additional resources would have brought you if invested clearly in the investment side?

Mr. BROWN. Well, I can just point to returns on investment generally from our ACS program, and generally the return on investment would be about 13 to 1.

Mr. POMEROY. 13 to 1.

Mr. BROWN. I have to point out that the returns are different because of the tools that we have.

Mr. POMEROY. Right. The tools you have are better.

Mr. BROWN. Our tools, yes.

Mr. POMEROY. I will introduce into the record additionally the envelopes used by some of your private collection agencies that are supposed to trigger this taxpayer response. In the corner of one, it says 131 Tower Park, Suite 100, PO Box 1800 Waterloo, Iowa. Is that your return address there, Mr. Penaluna?

[The information is being maintained in the Committee files.]

Mr. PENALUNA. Yes, sir.

Mr. POMEROY. On another one, another contractor, apparently P.O. Box 50, Perry, New York. They are in plain envelopes as the record will show. I will tell you what; either one of these come to my house, it would end up in the garbage can. I would figure it would be some unwanted credit card solicitation or something. I would just ask the IRS collection representative from Buffalo, now when you send out a letter, what does the envelope look like?

Ms. PARAY. It is an official Internal Revenue Service envelope.

Mr. POMEROY. An IRS envelope?

Ms. PARAY. Yes.

Mr. POMEROY. Then that is followed up with a call where the caller identifies themselves from the IRS?

Ms. PARAY. Yes, sir.

Mr. POMEROY. Commissioner, back to your point, when you talk about the tools available to the service, pound for pound, the service is going to collect more dollars if you are doing it with an in-house employee versus an outsourced employee.

Mr. BROWN. Yes.

Mr. POMEROY. In fact, having spent \$71 to make \$20, well, that is not nearly a 13-to-1 ratio. Now, let's talk about—

Mr. BROWN. This program will be 4 to 1.

Mr. POMEROY. This program hopefully will be 4 to 1.

Mr. BROWN. That is correct.

Mr. POMEROY. Although I would say the only 4 to 1 ratio I am aware of so far is that it costs four times what the commissioner advertised, what he testified here. That is the 4 to 1 ratio I see. You have got a commissioner who said it would cost \$13 million. It costs \$71 million to get up and running, and so far we haven't even brought in \$20. This is a loser.

What we ought to do is recognize the 10-year score repealing this program contemplates that all of the investment made is going to go away from collection. Well, if—we would turn this to a positive score in a heck of a hurry if we ditch 4-to-1 private collection and go to 13-to-1 public collection. If there is anything inherently governmental, it is the collection of revenues necessary to sustain the government. This runaway ideology we have to outsource everything the government does is costing taxpayers a lot of money to enrich a few private bill collectors, while subjecting taxpayers to private bill collectors on what ought to be a government responsibility.

Thank you, Mr. Chairman. I yield back.

Chairman RANGEL. Thank you. Mr. Van Hollen.

Mr. VAN HOLLEN. Thank you, Mr. Chairman.

At this point in the hearing, obviously a lot of territory has been plowed. So I am not going to go into great detail on a number of issues, and try to get back to sort of the basic framework you started with with the opening statement of the Chairman.

I would say, Mr. Brown, you pointed out that this was as a result of a congressional initiative. Just for the record, this was a provision that was tucked into a bill, hundreds of pages long originally, a number of years ago called the American Jobs Creation Act. It was rushed through the House without Members having an opportunity to vote up or down on this particular provision. In fact, the one time the House did have a chance to vote on this provision was when I joined with my colleague, Congresswoman Shelley Moore Capito, and offered an amendment to the Treasury appropriations bill to deny funding for this program. It was actually accepted on a voice vote by both the Republican floor leader and the Democratic floor leader.

So, the one time that the Congress—the House has gone on record on this particular issue has been in opposition to this particular program.

Now let me just ask—go back to the big picture. I think the testimony has been undisputed, Mr. Brown, that you agreed with the statements made by your predecessor, Mr. Everson, which is that this could be done more efficiently -this tax collection could be done more efficiently by the IRS if you are given the resources; is that not right?

Mr. BROWN. Yes. I would hasten, we would not put our next dollar on this slice of work. We would work on more complex cases, higher-priority cases.

Mr. VAN HOLLEN. Which could potentially collect more money for the taxpayer.

Mr. BROWN. That is correct. But I would ignore this slice.

Mr. VAN HOLLEN. Right. But, were you given the resources to do it, you agree with your predecessor that you could do it more efficiently; is that right?

Mr. BROWN. Yes.

Mr. VAN HOLLEN. I heard on both sides of the aisle one of the principles of our tax collection should be the efficient collection of taxes for the American people. Wouldn't you agree that that should be one of the priorities?

Mr. BROWN. We strive for that every day.

Mr. VAN HOLLEN. Okay. Is there anybody on this panel who contests the fact, the testimony of Mr. Brown and his predecessor, that giving the IRS resources to have these taxes be collected is not the most efficient way?

Okay. So, I would assume that putting aside your hats as representatives of different—but just as taxpayers, you would agree, I think everybody, that the American taxpayer gets the best return if the IRS is given the resources to collect this money; is that not right?

Mr. BROWN. I agree with that.

Mr. VAN HOLLEN. It seems to me the other theme here, in addition to efficiency, is fairness. We want a system that is both efficient and we want a system of collection that is fair.

I go back to another bill that Congress passed in the 1990s regarding tax collection that was mentioned in the Chairman's opening statement, that IRS agents are prohibited by law from being compensated based on the amount they collect. Is that not right?

Mr. BROWN. That is correct.

Mr. VAN HOLLEN. Now, I understand that in the contracts of the private debt collectors, the individuals do not get particular bonuses based on the amount they collect. But there is no doubt, right, Mr. Penaluna, that the return, the profit to the company, is obviously based on the amount you collect. Is that not right?

Mr. PENALUNA. That is correct.

Mr. VAN HOLLEN. As I understand the contracts, of the amounts that you collect, is it 25 percent that you are allowed to keep?

Mr. PENALUNA. It varies between 21 and 24 percent.

Mr. VAN HOLLEN. Okay. So, out of every dollar you collect through this process for the public, you get to keep between 21 and 24 cents; is that right?

Mr. PENALUNA. Well, there are certain accounts that are noncommissionable that we get a zero fee for. But generally speaking, the ones we do get fees for are between 21 and 24 percent.

Mr. VAN HOLLEN. It is natural—I think anybody in the country would expect a for-profit company to try to maximize their profits. But there does seem to be a tension here, because the extent to which the company makes or does not make a profit is obviously based on the amount collected. The reason we have in place all these protections for the taxpayers is to prevent overly aggressive collection tactics.

Let me just close with this question for Ms. Olson. I want to commend you for your work on this because it goes to the training issue of employees. Because, clearly, the more training people have in terms of the fair practices, the better off our constituents will be and the American taxpayers will be.

In your report you mention the fact that the private debt collection employees receive limited training and also experience high

turnover. Can you talk about that and the impact you think that has on the fair collection of these—

Ms. OLSON. What we found was that among the collectors themselves, or the collectors/tax specialist, whatever they called them, that there was a turnover of 20 to 50 percent. So that means that if you get, you know, you don't—you are not on the job long enough to understand that tax debts are different from other debts; how you need to work with taxpayers; or really have reinforced—get second rounds of training. You just have one shot of training. You are on the contract for a short period of time, and then you are off again.

That is so different from IRS employees, where over 77 percent of IRS employees in ACS have been there for—or CSRs rather—the people who can do installment agreements or the equivalent to the PCAs have been on the job for over a year and have gotten duplicate training.

Mr. VAN HOLLEN. I thank you all. Thank you, Mr. Chairman.

Mr. HERGER. Are we concluding?

Chairman RANGEL. Yes, we are concluding.

Mr. HERGER. Thank you, Mr. Chairman. I think this has been a very informative hearing.

I would just like to conclude just with what I have heard is what our goal is here. Our goal is we have a tax gap. We have people who are not paying their taxes after being—receiving multiple notices from the IRS. We are looking at a way to try to bring some of that in to help reduce the burden on all the—the vast majority of all taxpayers who are paying their taxes. I think it behooves us to look at anything we can to make this work.

It seems to me that as a pilot program we want to ensure that we give this enough time to see if it can work. We are basically taking those who aren't paying and allowing at least the private sector, being supervised in a proper way after making mistakes, we need to correct those mistakes; that we need to be, I believe, doing whatever we can in a judicious, fair way to get this money in. So, I personally would like to see this program continued long enough to see whether indeed it will work or won't work.

Thank you, Mr. Chairman.

Chairman RANGEL. Thank you. Let me thank Mr. Van Hollen and John Lewis and the staff for the excellent job they have done in focusing attention on what I consider a very serious problem.

I don't know about most American taxpayers, but I think there is a very special relationship between the Internal Revenue Services and the taxpayer. I would like to be able to talk to my government if I have a problem in collections; say, can we talk? I don't want that person motivated by how much money the private company can get. I want that person and only that person to have all of my personal records there to understand the ups and downs I have had, how much I owed, what I have tried to do, and to be my friend, because they too are being paid by the U.S. Government.

Whenever I have complaints—and I have many, coming from taxpayers—I tell them go to the Internal Revenue, they are there to help you. I find it very very difficult, no matter what their motivation is, to send them to somebody whose profit margin is going

to be dependent on, not whether they help the taxpayer but, how much money they get from the taxpayer.

Now, it just seems to me, Mr. Brown, that if you agree with your predecessor that you have more resources, you have the information, you can do the job cheaper and more effectively. Going into another contract would not only be the wrong thing to do but would go against the testimony that we received today.

So, as we conclude, is there anything that you have found out since you have given your testimony to Mr. Van Hollen that would indicate that your shop can't do a better job than what you are about to contract out to other people?

Mr. BROWN. No. I stand by Commissioner Everson's testimony. We are more efficient at this. Again, we have more tools the private debt collectors don't have.

Chairman RANGEL. I have to tell you that we are from the Congress and we are here to help, but we are on the same team. Your taxpayers are our constituents. They get annoyed. Guess what? We get annoyed. If there is a better way to do it, we don't want to tell you how to do it. We want to work with you and to do it.

So, how long are these proposed contracts that you are thinking about putting out for bids?

Mr. BROWN. Five-year contract, renewable annually.

Chairman RANGEL. That is not fair. I am 76 years old. That is almost unfair. I will never be able to see what happened.

Let's see whether or not we can be partners in government and work this thing out, so that, at the end of the day, the taxpayer is the winner.

Let me thank all of you for the hard work that you put into this hearing. Believe me, I am not just motivated by the efficiency and the cost savings. I don't like debt collectors, period. I don't like for them to know more about my private business than they should. I don't like them telling me the things that have been going on. Yet, I will accept it from the Internal Revenue Service, and our tax system is based on voluntary compliance, are a faith and belief that the Service is on their side. With all due respect to the private collectors, they don't enjoy the same reputation.

Let me thank all of you for your participation and I look forward to working with you. Mr. Brown, the quicker we get together the better. When do you come up for confirmation?

Mr. BROWN. I am sorry. I am just an acting commissioner. You would have to address the questions about who will be the confirmed commissioner to the White House or to Treasury, sir.

Chairman RANGEL. Well, I really look forward to working with you. Thank you.

[Whereupon, at 12:49 p.m., the hearing was adjourned.]  
[Submissions for the Record follow:]

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#### Statement of ACA International

Thank you for providing ACA International, the Association of Credit and Collection Professionals (ACA), the opportunity to submit written comments regarding the public-private partnership between the Internal Revenue Service (IRS) and private collection agencies. The following comments are respectfully submitted in response to several questions raised during the recent oversight hearing and comments made

by key lawmakers about the public-private partnership between the IRS and private collection agencies.

#### **ACA International**

ACA International is an international trade organization originally formed in 1939 and composed of credit and collection professionals that provide a wide variety of accounts receivable management services. Headquartered in Minneapolis, Minnesota, ACA represents approximately 6,500 company members based in more than 55 countries and includes credit grantors, third-party collection agencies, attorneys, and vendor affiliates. ACA has numerous divisions or sections accommodating the specific compliance and regulatory issues of its members' business practices.

#### **Being a Private Debt Collector**

ACA members range in size from small businesses with a few employees to large, publicly held corporations. Together, ACA members employ in excess of 100,000 workers. These members include the very smallest of businesses that operate within a limited geographic range of a single town, city or State, and the very largest of national corporations doing business in every State. The majority of ACA members, however, are small businesses. Approximately 2,000 of the company members maintain fewer than 10 employees, and more than 2,500 of the members employ fewer than 20 persons. Many of the companies are wholly or partially owned or operated by minorities or women. ACA serves members and represents the industry by developing timely information based on sound research and disseminating it through innovative education, training and communications.

As part of the process of attempting to recover outstanding payments, ACA members are an extension of every community's business. They represent the local hardware store, the retailer down the street, and your family doctor and State and local Government Nationwide. Many are approved government services contractors and collect debt for the Department of Education, the U.S. Treasury and all Federal regulatory agencies including, most recently, the Internal Revenue Service.

ACA members work with these businesses, government entities and regulatory agencies, large and small, to obtain payment for the goods and services received by consumers. Together collection agencies returned \$39.3 billion to U.S. businesses in 2005, representing a 22% reduction in private sector bad debt.<sup>1</sup> The \$39.3 billion returned to businesses was equivalent to an average savings of \$351 per American household, had businesses been forced to charge higher prices in the absence of debt recovery.<sup>2</sup> Additionally, during this same period, collection agencies returned \$693.5 million to Federal, State and local Governments in public sector bad debt.<sup>3</sup> Even with this effective private collection process, each American family pays \$2,200 per year to compensate for unpaid Federal income tax debt.<sup>4</sup> Through the combined effort of private collection agencies, billions of dollars are recovered annually, returned to business and government and reinvested. Should the use of professional collection agencies by private business and Federal, State and local Government be curtailed, the economic viability of these businesses as well as government—and by extension—the American economy in general, is threatened. Moreover, without the partnership between private business and professional collection agencies and the partnership between government and professional collection agencies, Americans will be forced to pay even more to compensate for uncollected debts, including tax debt.

#### **The Fair Debt Collection Practices Act**

During the hearing, several members of Congress posed questions about the collection practices of the agencies that are currently collecting uncontested tax debt on behalf of the IRS. The questions pertained to the absence of return addresses on collection notice envelopes identifying the IRS collection agencies, the failure of the collection agencies who presently collect uncontested tax debt on behalf of the IRS to disclose their identities when communicating with consumers by telephone, the need for the collection agencies to establish the identity of the called party before discussing the purpose of the call and the time of day when such calls are

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<sup>1</sup> "The Value of Third-Party Debt Collection to the U.S. Economy: Survey and Analysis," PricewaterhouseCoopers, June 2006.

<sup>2</sup> *Id.*

<sup>3</sup> Financial Management Service, U.S. Department of Treasury, *Fiscal Year 2005 Report to Congress on U.S. Government Receivables and Debt Collection Activities of Federal Agencies*, March 2006.

<sup>4</sup> National Taxpayer Advocate 2006 Annual Report to Congress.

placed to the indebted taxpayer. The answers to each of these questions lie within the text of the Fair Debt Collection Practices Act (FDCPA).<sup>5</sup>

Although members of ACA are subject to a host of Federal and State laws and regulations regarding debt collection, as well as ethical standards and guidelines established by ACA, the premier law controlling the conduct and communications of third-party debt collectors is the FDCPA. The FDCPA was passed with the support of ACA in 1977, to put a stop to unfair and abusive tactics and to balance the playing field between those debt collectors who collect debt in an ethical, consumer sensitive manner and those who may engage in unscrupulous debt collection activities.

This Act prohibits third-party debt collectors from engaging in deceptive or abusive conduct in the collection of consumer debts incurred for personal, family, or household purposes including tax debt. In order to protect a consumer's privacy, the FDCPA prohibits private debt collectors from disclosing the existence of debt to anyone other than the consumer. The statute accomplishes this by regulating with whom and how collectors can communicate. According to § 1692c(b) of the FDCPA, without consumer consent, "a debt collector may not communicate, in connection with the collection of any debt, with any person other than the consumer, his attorney, a consumer reporting agency if otherwise permitted by law, the creditor, the attorney of the creditor, or the attorney of the debt collector." By definition, a consumer includes the consumer's spouse, parent (if consumer is a minor), guardian, executor or administrator.<sup>6</sup> The disclosure of the existence of a debt to anyone other than the consumer who is obligated to pay the debt is a serious violation of the FDCPA. For the private collection agencies participating in the IRS's tax collection program, this means they cannot disclose they are calling on behalf of the IRS until they have verified they are speaking with the consumer or another permissible third party.

Further, a debt collector is prohibited from communicating with consumers by mail using postcards or envelopes with language or symbols that disclose the letter is from a debt collector and, by extension, the possible existence of debt.<sup>7</sup> To ensure compliance with this section of the FDCPA, all written communications from the private collection agencies must be approved by the IRS prior to use.

The FDCPA also prohibits debt collectors from contacting consumers at inconvenient hours. They may only contact consumers between the hours of 8:00 a.m. and 9:00 p.m.<sup>8</sup> They may not subject consumers to repeated telephone calls with the intent to harass.<sup>9</sup> Debt collectors may not threaten legal action or any other remedy available at law that is not actually authorized and contemplated.<sup>10</sup> Finally, under the FDCPA, third-party debt collectors must adhere to strict requirements concerning consumer disputes and validate debts as required by law.<sup>11</sup>

Of noteworthy importance to this body's understanding of the FDCPA, is the fact the FDCPA is a strict liability statute. Even the most arguably minor infraction of the FDCPA entitles the injured consumer to act as a private attorney general and initiate legal action against the debt collector.<sup>12</sup> This consumer right is preeminent. It exists regardless of the severity of the alleged violation or the intention of the debt collector. If successful, a consumer/plaintiff shall be entitled to his or her actual damages, statutory damages up to and including \$1000 and attorney's fees and costs.<sup>13</sup> But when enacting the FDCPA, Congress also recognized that even the most well-intentioned, conscientious, professional debt collector is fallible. In order to balance the severe penalties that may be imposed by a court of law on the debt collector who violates this strict liability statute, Congress provided debt collectors with a defense to an action alleging an FDCPA violation known as the bona fide error defense. The bona fide error defense provides the debt collector /defendant with the opportunity to show the court that the alleged violation occurred notwithstanding the fact the debt collector maintained reasonable procedures likely to prevent such violation of the FDCPA from occurring.<sup>14</sup> It is within this complex legal framework that debt collectors must operate, including those agencies that collect past due, uncontested Federal income tax.

<sup>5</sup> 15 U.S.C. §§ 1692–1692p (2006).

<sup>6</sup> 15 U.S.C. § 1692c(d) (2006).

<sup>7</sup> 15 U.S.C. § 1692f(7)–(8) (2006).

<sup>8</sup> 15 U.S.C. § 1692c(a)(1) (2006).

<sup>9</sup> 15 U.S.C. § 1692d(5) (2006).

<sup>10</sup> 15 U.S.C. § 1692e(5) (2006).

<sup>11</sup> 15 U.S.C. § 1692g (2006).

<sup>12</sup> 15 U.S.C. § 1692k (2006).

<sup>13</sup> 15 U.S.C. § 1692k(a) (2006).

<sup>14</sup> 15 U.S.C. § 1692k(c) (2006).

### **Understanding the IRS-Private Collection Agency Relationship**

Collection agencies, by definition, are the agents of their principals. They function on behalf of their clients, including their government clients, and do not act independently or without oversight. As a result, third-party debt collectors must at all times act in accordance with the instructions given by their client on each account and the terms of their contract of engagement. From time to time the client may ask to review a collection agency's work process (letters, phone calls, etc.) and set parameters as necessary to ensure the agency's efforts are in line with the client's goals. Therefore, under the IRS-private collection agency program, collection agencies are not only regulated by State and Federal laws and ACA, but also are regulated by the terms of the government's contract requirements and by reference, the IRS's own collection rules. In short, the private collection agencies collecting on behalf of the IRS are indeed the "agents" of their "principal" and act at all times under the direction and control of the IRS.

The relationship between the IRS employees and the private collection agencies retained under this program is symbiotic. By working together in a cooperative manner, the IRS employees and the private collection agencies will be able to meaningfully reduce the amount of unpaid, uncontested Federal income tax debt. The private collection agencies have not to date and will not in the future, displace IRS employees. Rather, they will be utilized by the IRS employees to collect the tax debt that would otherwise go uncollected and allow the IRS employees to focus their attention on the accounts that require IRS enforcement power, are subject to offer in compromise or are otherwise disputed by the taxpayer. As is the case in the private sector, the professional debt collector provides a service to the creditor and acts on the creditor's behalf. Private collection agencies do not become the creditor. So too is the case in point. The private collection agencies under contract with the IRS are positioned to provide a service to the IRS and act on its behalf. They are not positioned to become the IRS.

### **Tax Collection is NOT Tax Assessment**

Some have queried whether the use of private collection agencies to collect uncontested past due Federal income tax debt is an abrogation of the Federal Government's exclusive, constitutional power to assess income tax. ACA believes the assessment of Federal income tax is indeed an inherent function and power of the U.S. Federal Government. However, ACA strongly disagrees that the IRS's use of private collection agencies to assist in the collection of past due, uncontested tax debt abrogates their tax assessment and enforcement power in anyway.

Under the existing program, the IRS's use of private collection agencies is nothing more than the IRS's use of any other tool to collect past due tax debt. Like stamps on envelopes, telecommunication hardware, desks, computer system software or even paper, the private debt collectors are tools for the IRS employees to utilize on their behalf. In all instances, the tax debt subject to the private debt collection program was previously assessed by the IRS. In all instances, any discrepancy or dispute involving the assessed tax debt was previously resolved through communications between the IRS employees and the taxpayer before such debt was eligible for assignment to the private collection agencies for servicing. In all instances, the private collection agencies that perform services on behalf of the IRS under the program are only authorized to locate taxpayers, contact taxpayers and request and accept payment, either in full or in installments from taxpayers. Should any taxpayer have a question, concern, complaint or problem, they are immediately directed to the IRS. In no such instance does the private collection agency have the power to negotiate the amount due or initiate enforcement action. This means the efforts of the private collection agencies are a mere complement to the efforts of the IRS employees to collect this uncontested tax debt. They are not replacing IRS jobs nor are they engaging in collection practices that could be considered "inherently governmental."

In case this fact needs restating, the power to assess tax, negotiate amounts due, issue liens, seize property, garnish wages or initiate any other type of enforcement action remains solely with IRS under the program. The updated data on the taxpayer's whereabouts, as provided by the private collection agencies, belongs to the IRS. Despite the restrictions imposed by the FDCPA and the contract requirements of the IRS-private collection agency partnership, the private collection agencies performing under contract have already recovered \$19.49 million in delinquent taxes

as of April 28, 2007.<sup>15</sup> This is a program that should be applauded by Congress, embraced by those taxpayers who pay their fair share and heralded as a model for collection of uncontested, past due tax and government debt nationwide.

*Contact Information:*

Rozanne Andersen, CAE Senior Vice President, Legal and Government Affairs

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**Statement of American Association of People with Disabilities**

Mr. Chairman and distinguished Members of the Committee, I appreciate this opportunity to comment on the Internal Revenue Service's (IRS's) use of private debt collection companies to collect Federal income taxes.

I am here today on behalf of the American Association of People with Disabilities (AAPD). AAPD is the largest national nonprofit cross-disability member organization in the United States, dedicated to ensuring economic self-sufficiency and political empowerment for the more than 50 million Americans with disabilities.

As we prepare to recognize the 17th anniversary of the Americans with Disability Act (ADA) this July, there is little to celebrate in terms of the employment opportunities available to Americans with disabilities. While the national unemployment rate stands at about 4.7 percent, more than two thirds of working age disabled people in the U.S. are currently without a job. And the number of people with severe disabilities is increasing daily. Many of the men and women who have served their country proudly in Iraq and Afghanistan are coming home with severe injuries. The high number of returning disabled American veterans will only serve to compound this already staggeringly low employment rate within the disability community.

But Mr. Chairman, let me be clear—people with disabilities do not want a handout. We want to help ourselves. Today, more than ever, many jobs can be easily and readily adapted for people with disabilities by means of assistive technology. Unfortunately, discrimination and stereotyping are still barriers to many members of this community who are trying to return to or enter into the workforce.

The fact of the matter is that companies that currently have hiring programs for workers with disabilities have found that training and employment costs for those employees are offset by existing programs and resources including the WOTC tax credit. The small initial potential increase in employment costs associated with hiring persons with disabilities more than pays for itself over the long run in reduced employee turnover and lower training costs. Research shows that people with disabilities typically are exceptionally loyal employees, remaining on average nearly four times longer than their non-disabled counterparts.

When Congress enacted the American Jobs Creation Act of 2004 (P.L. 108-357), it created a unique opportunity for the Federal Government to stimulate creation of well-paying jobs for disabled veterans and other persons with severe disabilities. The Act contains provisions that allow for the IRS to enter into contracts with third-party debt collection companies in order to collect past due Federal income taxes.

Employment at third-party debt collection agencies can translate into high-paying careers. These jobs pay anywhere from \$25,000 to \$150,000 a year, with most averaging \$40,000. These positions also include health and 401(k) benefits. Individuals with significant disabilities who take these jobs will no longer rely as heavily on government benefit subsidies from SSI or DI, Medicaid and Medicare. This would not only help to alleviate the current low employment rate of persons with disabilities, it would also generate substantial savings.

On January 25, 2007, Senator Ben Nelson of Nebraska introduced S. Amdt. 208, the Disability Preference Program for Tax Collection Contracts, to H.R. 2, the Minimum Wage Act of 2007. The amendment would require that on all Qualified Tax Collection Contracts, a minimum of 15 percent of persons with disabilities be employed by contractors. The specific numerical goal would apply to aggregate employment across all contracts, not to individual contracts. This provision recognized that not all contractors may be able to meet the 35 percent standard for the preference, but that all contractors should be able to contribute to the goal of increased hiring of people with severe disabilities.

While I understand that there is opposition, for various reasons, to the IRS' outsourcing program, I would ask that you consider the positive impact that Senator Nelson's initiative would have across the board. An employment initiative such as the Disability Preference Program would provide a much needed demonstration to

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<sup>15</sup> Statement of Kevin M. Brown, Acting Commissioner, Internal Revenue Service, Testimony Before the House Committee on Ways and Means, May 23, 2007.

government contracting entities that similar contracting requirements should be used to provide good job opportunities for disabled veterans and other persons with disabilities.

Mr. Chairman, nearly 17 years ago this country made a commitment to the disability community by enacting the ADA. The Disability Preference Program will help us make good on the promise to promote equal employment opportunities for Americans with disabilities and will allow this country to honor those who have sacrificed so much on our behalf.

Thank you for this opportunity to present my views. The AAPD welcomes your comments and looks forward to working with the Members of the Committee on behalf of the more than 50 million individuals with disabilities and their families.

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**Statement of James Wallace, Allied International Credit**

Allied International Credit Corp., (U.S.) testified before the Ways and Means Subcommittee on Oversight four years ago in support of legislation to authorize the Internal Revenue Service to partner with the private sector to collect debts owed to the people of this country. We appreciate the opportunity to comment on the initial phase of the private debt collection program implementation.

In our testimony four years ago, we noted that the substantial resources and private sector best practices, expertise, and experience brought to the table by debt collection companies would help the IRS increase the number of cases resolved and shorten the resolution time. We said, "because the program will promote a greater reliance on case management, rather than on harsh collection activities such as seizures, levies, and garnishments, the program will make the tax compliance system fairer and more tolerable to taxpayers." In fact, as you know, the program authorized retains enforcement actions as the sole purview of the IRS, with the private debt collectors locating the delinquent taxpayers and eliciting payments from them. If, however, they are unable or unwilling to pay what they owe, the debt collectors provide the information and intelligence gained through the contacts to enable IRS to determine the appropriate actions to take.

In 2004, Congress authorized the IRS to use private collection agencies (PCAs) to collect back taxes from a subset of taxpayers with outstanding, undisputed tax liabilities. A limited implementation phase is underway. Administration and Congressional interest in closing the tax gap has only intensified since then. The tax gap has been the focus of hearings in both the House Ways and Means and Senate Finance Committees; the Administration has proposed 16 initiatives in its FY08 Treasury budget submission to close the tax gap; and the Treasury has been asked to develop a more aggressive strategy for reducing the tax gap even further.

While there is no single solution that will close the tax gap, the private collection initiative is closing cases, collecting monies owed, and gaining useful insights for IRS about delinquents. As we said in our testimony four years ago, "There will be a strong message that if you owe, you will not be ignored, increasing the incentive for taxpayers to meet their obligations sooner rather than later."

According to Acting Commissioner Kevin M. Brown, as of April 28, 2007, PCAs collected \$19.49 million in gross revenue. He also said IRS placed 3,973 cases with private collection agencies that have since been paid in full, and IRS has approved 1,467 installment agreements on PCA pursued cases. The IRS expects to recoup all of its costs for the program, including sunk costs, in April 2008. For funds allocated in FY 2007, all costs were recouped by April 2007.

AIC welcomes the close scrutiny of this program has received. PCAs should be held to the highest standards in collecting delinquent Federal taxes. PCAs have fared well under objective scrutiny from Government Accountability Office (GAO) and Treasury Inspector General for Tax Administration (TIGTA), and have consistently met or exceeded standards and expectations. Unfortunately, some of the criticism that has been leveled against the program is without merit or basis in fact.

Some have claimed that it would cost the IRS three cents to collect a dollar in unpaid taxes, while PCAs are being paid 21 to 24 cents on the dollar. Data from TIGTA indicates than when measuring comparable costs, the cost for an IRS revenue officer to collect \$1.00 in unpaid taxes is as high as 31 cents. Hiring more IRS revenue officers would involve recruiting, training, paying salaries, providing benefits and pension coverage, and overhead costs, such as office space, computers, and telephone service. Further, as IRS has experienced, dramatic increases in the collection workforce places a temporary drag on the revenue officer cadre until the new employees can be trained and assimilated into the workforce and become fully productive.

Funds collected by PCAs go directly to the IRS. Because the PCAs do not earn anything on accounts that make payments within ten days of being contacted by the PCA, the effective rate for PCAs is about 18.5 cents on the dollar, not the 25 cents on the dollar authorized by Congress.

If the Congress were to appropriate more funds for collection enforcement, the money would not be used to collect the delinquent accounts that are being collected by PCAs. As then-Commissioner Mark W. Everson told the Oversight Subcommittee on March 20, 2007, "It is not realistic to expect that the Congress is going to give the IRS an unlimited budget for enforcement, and if Congress provided the IRS additional enforcement resources, I believe those resources would be applied best by allocating them to more complex, higher priority cases that are not appropriate for PCAs."

Acting Commissioner Brown was even more direct, "In other words, the issue is not whether the IRS or PCAs can do a better job in collecting this revenue. The issue is whether the revenue is collected by PCAs or goes uncollected. If the program ceased today, the money we are currently investing in the PCA program would not be reassigned to IRS employees who would then pursue these cases."

Whether you believe the return to the government is greater if the IRS collects these debts or if PCAs do, if the dollar is not collected, the return to the government is the same: zero—which is also the degree of deterrence exerted on delinquent or potentially delinquent taxpayers.

As the initial implementation phase draws to a close, the IRS and the Congress will be able to build on this experience and learn how the program can be improved. In evaluating the program, it will be important to compare apples to apples and to remember that with the accounts turned over the PCAs, the question is not who can collect for less, but whether the delinquent taxes will be collected at all and delinquency will be deterred.

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#### Statement of Rothman

Let me begin by thanking the Committee on Ways and Means for allowing me to submit a statement for the record on this critical issue. I want to especially recognize the leadership of Chairman Charlie Rangel. Under the Chairman's stewardship, this Committee is once again protecting American taxpayers and I thank him for his great work.

Mr. Chairman and members of the Committee, I have long worked on this issue and thank you for taking up the important matter of the privatization of tax collection. When the Republican-led Congress attached a provision onto H.R. 4520, the American Jobs Creation Act of 2004, it allowed the IRS to hand over the tax returns of millions of American taxpayers to private contractors to collect delinquent taxes. This provision has and will continue to wreak havoc upon our tax collection system and under the new Democratic majority, this provision must be reversed.

When debating this issue, it is important to consider the compensation rates of the private collection agencies selected by the IRS to perform the work of IRS employees. While it costs the government only three cents for every dollar to have an IRS employee collect taxes, the Bush Administration thought it was wise to authorize the payment of almost 25 cents for every dollar collected by a private contractor.

On January 9, 2007, in her annual report to Congress, the IRS's own National Taxpayer Advocate Nina Olson identified the IRS' private debt collection initiative as one of the most serious problems facing taxpayers and called on Congress to repeal the IRS's authority to use private collection agencies to collect Federal taxes. The Advocate's report illustrated why the IRS' private tax collection program wastes taxpayer dollars, invites overly aggressive collection techniques, and jeopardizes the privacy of American taxpayers:

*"The IRS' Private Debt Collection initiative is not cost efficient, adds unnecessary costs and burdens to taxpayers, diminishes the improved image of the IRS, and surrenders too many valuable components of our tax administration system. Therefore, Congress should repeal IRC § 6306 and thereby terminate the Private Debt Collection initiative."*

As the Committee may be aware, I offered an amendment to the Fiscal Year 2007 Transportation, Treasury, and Housing and Urban Development Appropriation bill, which received approval of the full Appropriations Committee, that sought to stop the IRS from proceeding with this ill-advised tax collection scheme. Unfortunately, because the Republican-led Congress failed to enact most of the Fiscal Year 2007 Appropriations bills, this Amendment was not enacted into law. I ask now for the

Committee on Ways and Means to do now what the previous majority failed to do, which is to stand up for taxpayers and for the integrity of our tax collection system.

Again, I would like to thank Chairman Rangel for his leadership on this issue and for allowing me to submit this statement for the record.

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#### Statement of Sierra Group

Please accept my testimony for the record regarding the major role that the Disability Preference Program for Tax Collection Contracts can play in reversing the negative employment trend for Americans with Disabilities, including recently injured Veterans, through the creation of 1000's of well paying jobs while successfully recouping millions of dollars in unpaid taxes.

#### Background:

U.S. Census statistics show that 10 percent of all Americans have a disability. Of that total, 27 million Americans have a severe disability that affects their ability to see, hear, walk or perform other functions necessary for the workplace. Assistive technology is enabling thousands of these individuals to work; however, the unemployment rate for people with disabilities remains more than eleven times the national rate. Seventeen years following the passage of the Americans with Disabilities Act, which was enacted to prohibit discrimination solely on the basis of disability in employment, public services, and public accommodations; the unemployment rate for people with disabilities remains at 70—80%. Additionally, more than 22,000 men and women are returning from the Iraq war, previously employed, now physically disabled, and in need of a totally different way to earn a living.

Assisting people with disabilities in finding and maintaining competitive employment is important to society. Despite the fact that a person's natural talent and ability can be turned into competitive work skills, American businesses seem to need a catalyst that will show them how to benefit from hiring people with disabilities. This catalyst that would begin to change the dire unemployment picture for these persons with disabilities is the Disability Preference Program for Tax Collection Contracts. Once enacted into law, the initiative will serve as a pilot program to demonstrate to business the benefits of bringing these men and women into the workforce, in large numbers. The Disability Preference Program for Tax Collection Contracts is very well suited to be this catalyst for several reasons, including:

- It will provide well paying jobs with health benefits and 401(k) benefits;
- It will provide jobs that require only a high school education or GED which is of particular import to returning veterans who have become disabled
- It will provide jobs that are well suited to accommodations, including use of assistive technology

In my 15 years of experience providing services for job seeking Americans with disabilities, and to employers who hire them, it is often difficult to find work that is so well suited for those with severe disabilities. The jobs that would be created by the Disability Preference Program for Tax Collection Contracts involve work from a desk, computer and telephone, all of which can be readily adapted for people with the most severe disabilities including mobility impairments, mild traumatic brain injury; severe vision loss and other impairments.

In addition, finding jobs with sustainable wages and benefits for individuals with a high school diploma or GED is difficult. Of individuals identified as both unemployed and having a severe disability, nearly 50% of them have an education that has not culminated in a high school diploma. In fact, nearly 40% of this total is educated at or below the 8th grade level. *The Journal of Rehabilitation* (July/August/September 2002, volume 68, Number 9) addresses the need for accommodations during GED testing for adults with disabilities because research demonstrates that people with disabilities ages 15 to 20 fail to complete high school at twice the rate as those without disabilities (41 percent vs. 21 percent). Therefore, those who go on to successfully gain their GED have even less opportunities than their non-disabled counterparts.

Given these facts and the opportunities offered by the proposed legislation, the Disability Preference Program for Tax Collection Contracts is a pilot program that is certain to succeed in putting thousands of severely disabled men and women to work in meaningful, well paying careers. The success of this program will serve as an example that can allow additional opportunities for additional governmental contracts to business to encourage the employment of people with disabilities, at good wages and with benefits.

This “business first” approach provides a reason to build upon the numbers of employees with disabilities a business includes in its workforce by offering an incentive during the contracting phase, in order to stimulate the hiring of a large number of qualified men and women with disabilities into our shrinking American workforce. The need for this program is further evidenced by the GAO Report in 2002 that found low numbers of businesses routinely using the Work Opportunities Tax Credit (WOTC), the Disabled Access Tax Credit (DAC) and the Architectural Barriers Removal Deduction. This study which I participated in, found that many businesses were unaware of the programs. I and others contacted recommended that Congress take steps to reach out to business to educate them about existing incentives.

I have seen first hand how leveraging assistive technology and training in a third party debt collection production center gives people with disabilities the opportunity to obtain the skills they need to be successful tax collectors, and provides them with solid customer service skills that will be transferable should they wish to move on to another career. Armed with this career experience, those now on the ranks of the unemployed will become self sufficient-taxpayers themselves, while acquiring valuable employment skills to use in their future.

Regarding the need to create jobs that can accommodate an assistive technology user, the National Organization on Disability (NOD) study in 1998 revealed that 25 percent of all people with disabilities who work use assistive technology. This same study also noted that 45 percent of those with disabilities who are unemployed stated that they would *require* assistive technology in order to become employed. Therefore, the Disability Preference Program for Tax Collection Contracts, as a pilot program, is well suited to allow this large group of people with severe disabilities to have a chance to work.

The Disability Preference Program for Tax Collection Contracts contains a requirement that 15 percent of employees hired by contractors in the aggregate across all contracts, be Persons With Disabilities, and this requirement will result in cost savings for the American Taxpayer and expanded job opportunities for disabled veterans and other persons with disabilities. For example, in the State of Nebraska, in 2005, about 5700 Persons With Disabilities were served by vocational rehabilitative services for employment services. Of that number, 1800 were hired or 31 percent. Thus, of the 3900 who remain seeking employment in Nebraska, if only 10 percent were qualified to work as collectors, that would be 390 people, and these numbers do not include veterans with disabilities who are traditionally served by a separate agency.

Nebraska's experience is replicated across the country. The U.S. Department of Education Rehabilitative Services Administration (RSA) 1999 Report regarding people with disabilities who would meet the definition contained in the Disability Preference Program for Tax Collection Contracts indicates that state vocational rehabilitation agencies have provided services to more than 1 million individuals with disabilities each year from 1995 through 1999. In 1998 and 1999 they provided services for 1.3 million individuals and in 1999 more than 85 percent had significant disabilities. Again, this number does not include those who are veterans, another group of Americans who struggle to find work once disabled.

Given this data, and the reasons outlined that indicate why debt collection is a job that many individuals with disabilities are qualified and able to perform, enactment of this program would make important progress on America's promise to veterans and other persons with disabilities to provide full access to our society.

Additionally, the Federal Government, the largest employer in the country, is traditionally looked to as the largest employer of people with disabilities. Unfortunately, at this time, the overall total of people with disabilities employed in our Federal Government is under 1 percent. This number is unacceptable in light of the assistive technology accommodations that can be made today. The Disability Preference Program for Tax Collection Contracts,—in a specifically targeted industry—will authorize the Secretary of the Treasury to create the structure to hire a targeted 15 percent of the overall, outsourced workforce, Persons With Disabilities, and therefore serve as a positive model for all private sector companies as well as a necessary example to our Federal Agencies.

In the last 15 years, with the improvements in technology, and assistive technology, The Sierra Group, Inc., has trained and assisted over 3,500 individuals. Sierra has an 80% success rate—success being defined as four years after an individual is provided with assistive technology or training for vocational and educational purposes, they are still utilizing the services provided. Every day in America, thousands of job seeking people with disabilities are turned away by businesses that have not seen the proof that these people can work. This travesty in unemployment must be reversed if we are to be a fully inclusive society that values diversity in our workforce. American businesses obviously need and require both a straight-

forward incentive and a successful pilot program to prompt them to recruit, hire, train, and accommodate workers with disabilities. Congress and the Federal Government have a unique opportunity to make this happen simply by passing the Disability Preference Program for Tax Collection Contracts.

#### **Statement of the Tax Fairness Coalition**

Chairman Rangel and Members of the Committee, thank you for holding today's hearing on the IRS' Private Debt Collection program. We appreciate the opportunity to share the views of the Tax Fairness Coalition about this program and respond to some of the concerns raised about this public-private partnership.

The Tax Fairness Coalition represents a group of private collection agencies committed to helping the IRS close the \$345 billion tax gap. The undisputed delinquent tax debt collected and returned to the U.S. Treasury can provide vital funds for government services while reducing the tax gap burden on the average American's tax bill.

Members of the Tax Fairness Coalition include AllianceOne Receivables Management, Inc., Allied Interstate Inc., The CBE Group, Inc., Financial Asset Management Systems, Inc., Linebarger Goggan Blair & Sampson, LLP, and Pioneer Credit Recovery, Inc. The CBE Group and Pioneer Credit Recovery are currently participating in the limited implementation phase of the IRS Private Debt Collection Program. The Coalition is a project of ACA International, an association of professional collection companies.

Since this program began in September 2006, the participating members of the Coalition have worked diligently to ensure that we just didn't meet, but exceeded the expectations of the IRS. When it comes to operations, we are going beyond the letter of the law and Section 6306 of the IRS.

Our professionalism and upfront investments in technology and training are paying off. To date, we have collected approximately \$20 million, earned exemplary customer satisfaction and professionalism scores, and have helped the IRS close the estimated \$345 billion tax gap.

Despite our success, some critics who do not believe this program should continue and expand. We obviously do not agree with their conclusions and appreciate this opportunity to set the record straight about how the program works, our successes, and answer some of the myths and rumors about the initiative.

This program has its origins in the American Job Creation Act of 2004 (P.L. 108-357), which allowed the IRS to enter into contracts with private debt collection agencies to recover delinquent taxes of relatively small assessed and undisputed tax amounts. The impetus for the program began as Congress looked for ways to reduce the \$345 billion tax gap. This enormous sum of money—which is the difference between the taxes owed and what's paid—creates a \$2,700 "tax gap burden" or surcharge for law-abiding taxpayers.

The IRS reviewed the credentials of 33 companies for participation in the initial phase of the program. Three companies were initially chosen to enter into contracts that began in September 2006. This limited implementation phase runs through March 2008. The IRS estimates that between \$1.5 and \$2.2 billion in delinquent tax revenue could be collected over a 10-year period through its Private Debt Collection Initiative.

This program also has a significant job creation element for the IRS. A portion of the funds that are collected go directly to the IRS to fund enforcement efforts, which may include hiring additional personnel. This element of the program is an area we feel the Congress may want to examine as a way to encourage more collection efforts at the IRS.

In addition to helping close the tax gap and creating new jobs at the IRS, the private collection agencies working on the contract are operating well, affording delinquent taxpayers all rights and protections provided under the law, as evidenced by the following successful outcomes:

- Customer service satisfaction—private collectors have achieved 95% satisfaction ratings, while IRS personnel have received ratings of 63.1 percent;
- Perfect score of 100% for professionalism and 98.1% for regulatory and procedural accuracy;
- Secure, monitored collection processes with no instances of abuse, loss or fraud with taxpayer information;
- Exemplary compliance in following all laws and regulations governing their collections activity; and

- Positive remarks and evaluations from officials charged with overseeing the program, including the Treasury Inspector General for Tax Administration and the Government Accountability Office.

According to a letter dated May 21, 2007 from Senator Charles Grassley to Treasury Secretary

Henry Paulson, the IRS' Return on Investment (ROI) "is about 4 to 1" on average—basically the same as the projected ROI for the Private Debt Collection program, which is estimated to be "between 4.0 to 1 and 4.3 to 1, once the program is in steady state." These new IRS figures are in stark contrast to past figures citing the IRS' ROI to be 10 to 1, 20 to 1, and higher. The numbers indicate that the PCAs are a cost-effective solution to collecting delinquent taxes. In other words, the IRS estimates it spends 25 cents for every tax dollar brought in, while the private collection agencies earn an average "effective rate" of 17.3 cents on the dollar.

As former IRS Commissioner Mark Everson and Secretary Paulson have stated in testimonies before Congressional Committees, the IRS Private Debt Collection program is helping to clear a backlog of cases that would not be touched by IRS employees, even if Congress provided substantial new resources to the IRS.

The private collection agencies' record in customer service and compliance is further proof of the critical service and invaluable assistance they provide to the IRS. The private debt collection agencies generate funds sent directly to the IRS that go to the U.S. Treasury to help reduce the tax gap. Indeed, without this important service, the tax gap would continue to grow.

#### **Tax Collection: Inherently Governmental?**

When the IRS Oversight Board met earlier this month to discuss the status of the IRS Private Debt Collection Program and the IRS FY2009 budget it reported that, "Overall, this program seems to be working well—Through this program, the IRS has found a way to reach a specific segment of the non-compliant taxpayer population."

This initiative is forward-thinking in the sense that private sector firms are being asked to partner with the IRS. With this in mind, however, it should be noted that the IRS actually lags behind many States and other Federal agencies that partner with the private sector to collect delinquent income taxes and other governmental debts such as non-tax delinquencies and defaulted student loans.

State governments and agencies have been working in partnership with private collection agencies for more than 25 years. Forty-one States currently employ private collection agencies to recover delinquent income taxes and other government debts. Thirty-four States collect delinquent income taxes. Hence, collecting delinquent taxes and other government fines is not an inherently governmental function. Rather, the use of professional collection agencies who have invested millions of dollars in technology and training is simply an efficient use of taxpayer dollars. In fact, the Congressional Research Service has determined in an analysis conducted in 2006 that the IRS use of private debt collection firms is not an inherently governmental function due to the very limited nature of the program's scope and authority provided to private collection firms.

In addition to complementing the IRS, other Federal Agencies, States, and localities in its own collections, private collection agencies have supported thousands of jobs nationwide. In 2005, private collection agencies employed 426,700 workers with a payroll of \$15 billion, according to the Bureau of Labor Statistics. As an industry, the private collection agencies returned \$39.3 billion in collections to the U.S. economy, saving the average American household \$351.

The reality is that if the private collection agencies were not collecting these delinquent taxes for the IRS, no one would. There are millions of Americans who owe acknowledge they owe Federal income taxes but have not been contacted by the IRS. Often, it simply takes one contact to have a taxpayer send in a check to the IRS or set up a payment plan that's been authorized by the agency. And when they pay within ten days of being assigned for collection to these firms, the companies working on the contract receive zero compensation.

These are not relatively large tax debts that are owed, either. Rather they average around \$5,000 going up to about \$25,000 and the amount owed is not in dispute. The problem is that the IRS does not—and will not anytime soon—has the staff or the required systems to contact these individuals as the private collection agencies can. The IRS takes a pyramid approach when it comes to collections and works on the larger debt cases first. Those more complicated and large collection cases required a level of sophistication for which the IRS and its professional staff are best suited.

Our efforts are complementary to the IRS. Not one single IRS employee has lost or will lose his or her job or be displaced because of this program. Indeed, this pro-

gram is structured so that it could fund additional IRS collections positions—and without an additional appropriation from Congress.

Members of the IRS Oversight Board alluded to this complementary effort in a recent release, noting that the IRS Private Debt Collection program “helps the IRS focus its resources on more complex cases.”

Furthermore, the IRS is authorized to use the first 25 cents of every dollar collected by the PCAs for enforcement efforts, including hiring new collection employees. Based on a previous analysis conducted by the Coalition, at current collection rates, about \$5 million will go to the IRS, which could fund 33 collection positions right now at the IRS. Based on the \$1.5 billion estimate, roughly \$60 million a year could then be available for the IRS to fund the employment of close to 400 new collection officers. This is based on the \$150,000 average cost to train, provide salary, benefits, bonuses, taxes and overhead for an IRS function collection officer, according to data from various Federal Government reports, including readily available data such as GS pay schedules and information from the IRS Oversight Board and TIGTA.

Clearly the benefits of this program only strengthen the IRS’ own efforts and encourage the Federal Government to be even more innovative in using and leveraging its resources to collect money it is owed.

#### **The Issue of Cost**

There has been much misinformation about whether the IRS could collect these delinquent taxes cheaper than private collection agencies. According to IRS data, the true cost of collections for the agency is about 25 cents on the dollar when one takes into account that, unlike private collection agencies, the IRS has available to them tools that the private sector doesn’t. These tools include the ability to compromise accounts, issue numerous automated demand letters and seizure of assets—both personal property and funds in bank and brokerage accounts—to satisfy a tax debt. Private collection firms do not possess these inherently governmental tools or powers—and are only authorized to set up voluntary payment arrangements with delinquent borrowers.

The companies participating in this initiative are actually recovering these tax debts at a cost of roughly 17.3 cents on the dollar. This “effective rate”—or their commission—is significantly lower than the 25 cents authorized as part of the companies’ contracts with the IRS. And the costs actually will continue to go down as the volume of cases the companies receives and handles increases.

From a cost perspective, the program is yielding significant results on behalf of the American taxpayer. The IRS has turned over 37,869 cases worth \$255 million in unpaid taxes to the PCAs since the limited implementation phase of the program began. To date, more than \$20 million has been collected with more than \$16 million going to the Treasury.

The program, as noted before, also helps fund IRS enforcement efforts, which could include hiring new collection personnel. So far, about \$5 million has gone to the IRS. This is a savings multiplier for the American taxpayer in that delinquent taxes are collected and funds are provided through the program for additional enforcement efforts to help close the tax gap and its associated \$2,700 per taxpayer burden.

#### **Securing Taxpayer Security and Ensuring Rights**

When it comes to protecting taxpayer data and ensuring their rights, the private collection agencies working on this contract takes its responsibilities seriously. Private collection agencies abide by even higher standards for security and privacy than those mandated for government collections programs. The PCAs taking part in the PDC program operate in accordance with IRS rules as well as the Fair Debt Collection Practices Act, Fair Credit Reporting Act, and all other applicable Federal and State collection and privacy regulations. Participant company employees—from collection personnel to managers to information systems personnel must pass an extensive background check.

To protect taxpayers’ privacy, the IRS provides PCAs with only the taxpayer ID number, address, tax year, and amount of taxes owed. PCAs use this limited information to contact taxpayers and help them enter into voluntary repayment agreements. Taxpayers’ tax returns, wage or employer information, and other sensitive taxpayer data never leave the IRS.

It should be noted that PCAs do not have the authority to compel an individual to speak with them. Taxpayers speak with private collection agency representatives voluntarily. When they are contacted, taxpayers are informed that they may also ask to have their case referred back to the IRS. According to the National Taxpayer Advocate’s 2006 Annual Report to Congress, only one-half of 1% of taxpayers con-

tacted by PCAs had requested to deal directly with the IRS. Also, less than one quarter of 1% of those taxpayers contacted by the PCAs have filed complaints with the IRS. Only one complaint, which was from a company not currently working on the program, was found to be valid by the IRS, according to the IRS Oversight Board.

In fact, the Treasury Inspector General for Tax Administration has singled out the program for diligently working to protect taxpayer data and ensure their rights. "Overall, the IRS effectively developed and implemented several aspects of the Program, thus providing better assurance that taxpayer rights are protected and Federal tax information is secure," according to a report issued by TIGTA in March 2007.

The report noted that "contractor employees were adequately trained, background investigations were completed, telephone call monitoring and oversight procedures were established, and computer and physical procedures were established before cases were assigned." Also, the report stated that contractors "implemented a strong system of computer and physical security controls."

TIGTA also stated that private collection agencies were receptive to recommendations for contract improvements and implemented them. Furthermore, security concerns were addressed prior to any tax cases being sent to the PCAs and "therefore, the contractors had not yet received Federal tax information."

This report clearly shows that the program is making progress collecting delinquent taxes in an ethical, professional, and security-focused way. Even though the contractors already had extensive security and privacy measures in place, there are always areas for improvement and as the report notes PCAs and the IRS responded promptly and effectively to TIGTA's additional recommendations to ensure the service delivers only the most ethical and strongest integrity while exceeding all financial and quality service expectations.

### **The Program's Future**

This Committee is keenly aware of our country's fiscal situation. Collecting every dollar counts when it comes to being able to fund current Federal Government programs and meet future challenges. This is where Private Debt Collection program comes into play.

Currently the program is in its limited implementation phase. It is a time to incorporate the lessons learned during this limited implementation phase and incorporate industry best practices to further enhance the tax collection system. When necessary improvements have been identified, as has been noted by independent government organizations, the IRS and the PCAs corrected them quickly and to the benefit of the taxpayer.

As we have stated before, this program complements the efforts of the hard-working people at the IRS. We do not wish, nor do we want, to be a replacement to this agency. Use of PCAs is only part of the solution and we encourage Congress and the IRS to develop a comprehensive set to programs and tools, including the continuation of the PDC program, to alleviate our national tax gap. Therefore, our future is simply based on the overwhelming numbers of cases that are out there that the IRS—even if it were to hire an additional 1,000 collection agents—would never reach. Each year it is estimated that \$20-billion goes permanently uncollectible because of the 10-year statute of limitations. We want to continue working with the IRS for the benefit of the American taxpayer.

